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Richard Madsen and Nancy Madsen, his wife, for themselves and all others similarly situated v. Washington Mutual Bank : Brief of Appellant

Utah Court of Appeals

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IN THE UTAH COURT OF APPEALS

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiffs and Appellants, vs. WASHINGTON MUTUAL BANK fsb, (successor to PRUDENTIAL FEDERAL SAVINGS and LOAN ASSOCIATION), Defendant and Appellee.	Case No. 20060597 - SC

BRIEF OF THE APPELLANTS

APPEAL
FROM THE THIRD JUDICIAL DISTRICT COURT
COUNTY OF SALT LAKE, STATE OF UTAH
HONORABLE LEON A. DEVER, JUDGE

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LIST OF PARTIES

The above caption of this case contains the names of all parties to the proceeding in the court whose judgment is sought to be reviewed. Throughout this brief, Madsen will refer to the defendant and appellant as "Prudential."

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JURISDICTION

Appellate Jurisdiction to the Utah Supreme Court is conferred pursuant to § 78-2-2(3)(j) of the *Utah Code*. The Utah Supreme Court has transferred the case to the Utah Court of Appeals pursuant to § 78-2-2(4). Accordingly, this Court now has jurisdiction pursuant to § 78-2a-3(2)(j).

STATEMENT OF THE ISSUES

The following issues are presented for review:

1. If a bank holds pledged funds and secretly earns profits on those funds, what statute of limitations, if any, applies?

The standard of review is one of correctness, since the trial court's application of the statute of limitations presents a question of law. *Estes v. Tibbs*, 1999 UT 52, ¶ 4, 979 P.2d 823. This issue was preserved below at R. 2714-20, 3013-20, 6366, 7610-16, 12744-7.

2. In 1979, the Utah Legislature passed a new statute (§ 7-17-4). Did the new statute (§ 7-17-4 U.C.A.) cut off class members' rights to profits earned on pledged accounts after June 30, 1979?

The interpretation of a statute is a question of law the appellate court should review for correctness. *N.A.R. v Elmer*, 2006 UT App. 293, ¶ 4, 141 P.3d 606. This issue was preserved at various places in the record, including R. 6872-76, 6975-84, 7258-64, 9104-12, 10838-48.

3. Is Madsen entitled to compound interest during the time that Prudential earned profits by using the pledged funds? If so, for what period of time would the

compounding continue? In the alternative, is Madsen entitled to prejudgment interest; and if so, for what time period?

This issue presents a question of law to be reviewed for correctness. *Carlson Distributing Co. v. Salt Lake Brewing Co., L.C.*, 2004 UT App 227, ¶ 15, 95 P.3d 1171; *Christensen v. Munns*, 812 P.2d 69 (Utah App. 1991). This issue was preserved at R. 3034-43, 6456-9, 7982-3, 12229-35, 12700.

4. Was it proper for the trial court to eliminate, from the previously certified class, duplexes, second homes, or commercial properties; even though the contract language was the same as the Madsen contract?

Whether the trial court applied the correct legal standard in reducing the size of the class is a legal question reviewed de novo. *Parker v. Time Warner Entertainment Co.*, 331 F.3d 13, 18 (2d Cir. 2003). This issue is preserved below at R. 5026-31, 5210-15.

5. Should the Master be disqualified and all of this work vacated because of his *ex parte* meetings with one party? And should the Master's work be vacated if it can be shown that he (the Master) relied on work done by others, rather than doing the work himself?

The standard of review is whether the trial court abused its discretion (perhaps as a matter of law) in refusing to disqualify the Master and in adopting the Master's report. *Plumb v. State*, 809 P.2d 734, 742-3 (Utah 1990). If there was abuse of discretion, this Court "must vacate the order unless the error was harmless." *Id.* at 741. "The standard

for determining harmless error is whether it is reasonably likely that the trial court's final order would have been different absent the master's improper activities." *Id.* at 744.

6. Because Prudential has not provided an acceptable accounting, in a case that is 32 years old, should this Court simplify matters and order that damages be calculated using the passbook savings rate of interest?

This issue is one for the appellate court only, and hence is a question of law. *Simper v. Scorup*, 78 Utah 71, 1 P.2d 941 (1931).

DETERMINATIVE LAW STATUTES, ETC., TO BE INTERPRETED

Utah Code Ann. § 78-12-34, states:

> To actions brought, to recover money or other property **deposited** with any bank, trust company or savings or loan corporation, association or society **there is no limitation**. (Emphasis added.)

Utah Code Ann. § 7-17-4(1):

> (1) A lender not requiring the establishment and maintenance of a reserve account shall offer the borrower the following options:
> (a) The borrower may elect to maintain a non-interest-bearing reserve account to be serviced by the lender at no charge to the borrower; or
> (b) The borrower may manage the payment of insurance premiums, taxes and other charges for his own account.

STATEMENT OF THE CASE

Madsen purchased a home in 1964. In order to finance the purchase, Madsen borrowed $16,800 from Prudential Federal Savings and Loan. The trust deed provided in part:

> In addition to the monthly payments as provided in said note, the TRUSTOR agrees to pay to the beneficiary, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said budget payments are hereby pledged to the BENEFICIARY as additional security for the full performance of this deed of trust and the note secured hereby. (R. 5.) (Emphasis added.)

Madsen claims that Prudential invested the "pledged" funds and earned a profit. (R. 931.) Madsen sued for an accounting of the profits. The lawsuit was filed as a class action, and the class was certified.

Early in the case, the trial court granted a summary judgment for Prudential dismissing the case. Thus followed the first appeal, *Madsen v. Prudential Federal Savings & Loan Assn.*, 558 P.2d 1337 (Utah 1977)[1] (included herein as Ex. A.) In *Madsen I*, the Utah Supreme Court reversed the trial court and remanded. The Utah Supreme Court held, *inter alia*, that:

> The pledgee has the duty to account to the pledgor for the increase or profits accruing to the pledgee as a result of the possession of the pledged chattel. *Id.* at 1340.

After the decision in *Madsen I* (above), Prudential removed the case to federal court. The federal court dismissed the action. Madsen appealed. *Madsen v. Prudential Federal Savings & Loan Ass'n*, 635 F.2d 797 (10th Cir. 1980).[2] (Included herein as Ex. B.) In *Madsen II*, the Tenth Circuit Court of Appeals held *inter alia* that:

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[1] Hereafter *Madsen I.*

[2] Hereafter *Madsen II.*

> Since no federal controversy was disclosed on the face of the Madsens' state court complaint, as amended, removal was improper and the consolidated case must be remanded to state court. *Id.* at 803.

After remand to the trial court, Judge Rigtrup held a bench trial. At the conclusion of the trial, Judge Rigtrup entered a verbal bench ruling in favor of Madsen. After the verbal bench ruling was issued (but before written findings could be entered) Prudential claimed that Judge Rigtrup was biased and should be disqualified. The presiding judge agreed and dismissed the case. Madsen appealed. *Madsen v. Prudential Federal Savings and Loan Ass'n*, 767 P.2d 538 (Utah 1988).[3] (Included herein as Ex. C.) The Utah Supreme Court reversed and remanded.

After the case was remanded, Judge Rigtrup entered written Findings of Fact and Conclusions of Law. (Included herein as Ex. D.) As part of the Findings of Fact and Conclusions of Law (Ex. D.), Judge Rigtrup ruled *inter alia* that:

> 10. Prudential should be ordered to pay to Madsen the sum of $134.70 for profits or earnings Prudential has realized by using Madsen's "budget" payments for the period of March 3, 1971 to June 30, 1979.
>
> * * *
>
> 12. All class issues are reserved for further proceedings. (R. 3003).

After remand, the trial court appointed a Master. The Master filed his final report, dated March 1, 2002. (R. 10370-2, included herein as Ex. G.) As part of his final report (Ex. G), the Master concluded that there were 9,547 class members; and that the average

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[3] Hereafter *Madsen III*.

damages per class member would be $105.18; resulting in a total judgment for all class members of $1,004,153. (R. 10371.) Based upon the Master's Report, the trial court entered a Final Judgment of $1,004,153 for the entire class. (R. 13842-3, included herein as Ex. I.)

Madsen appealed the trial court's Final Judgment. (R. 13850-83.) As part of this appeal, Madsen claims that the computation of damages by the Master should have been higher; and that the Master failed to account for all class members.

STATEMENT OF FACTS

The facts relevant to this appeal are set forth in the Findings of Fact entered by Judge Rigtrup. (See R. 2997-3001, Ex. D.) For purposes of this appeal, Madsen does not challenge any of the Findings entered by Judge Rigtrup. (Ex. D.) However, Madsen does challenge computations included in the Master's Report of March 1, 2002 (Ex. G herein).

SUMMARY OF ARGUMENT

Since this case deals with funds that were on deposit with a bank or savings and loan corporation, there is no statute of limitations. § 78-12-34, *Utah Code Ann.* Consequently, Madsen should have been awarded the profits earned from the time the deposit was made in 1964. At the very least, since the deposit was made pursuant to a contractual requirement, Madsen is entitled to the profits accruing during the six years immediately prior to the filing of this action in 1975.

In 1979, the Legislature passed the Interest on Mortgage Loan Accounts Act. Utah Code Ann. § 7-17-1, *et seq.* And Judge Rigtrup cut off damages as of 1979 because of

the Act. However, that Act did not apply to any action filed before 1979. Furthermore, Prudential did not comply with the terms of the Act; and the mandate of the 1977 Supreme Court decision had already established the law of the case in this matter.

Prejudgment interest is appropriate in this case because the amount of the pledge is "ascertainable at any given time," and evidence was presented which enabled the calculation of damages.

The class in this case was initially certified to include all borrowers having identical contract provisions with respect to money pledged for the payment of taxes and insurance. Late in the case, Judge Rigtrup removed duplexes, second homes and commercial properties from the class. By narrowing the definition of the certified class, the trial court not only violated the mandate, but dismissed a subclass without any notice to the members of the class.

The conclusions of the Master should be disregarded because the Master has stated that more testing needs to be done; thus, the Master's Report is not yet finishedl.

ARGUMENT

POINT I
THIS COURT IS BOUND TO FOLLOW THE MANDATE OF THE UTAH SUPREME COURT

As stated in the Introduction, this case has been to the Utah Supreme Court on two prior occasions. (See Ex. A and Ex. C.) Many of the issues before the Court on this appeal have already been decided on the two prior appeals. Under the doctrine of "law of the case," this Court is bound by the mandates of those two prior decisions.

> Law of the case terminology has been applied to a number of distinct sets of problems, each with a separate analysis. One branch of the doctrine, often called the mandate rule, dictates that pronouncements of an appellate court on legal issues in a case become the law of the case and must be followed in subsequent proceedings of that case. [citations omitted.] The lower court must not depart from the mandate, and any change with respect to the legal issues governed by the mandate must be made by the appellate court that established it [viz. the Utah Supreme Court] or by a court to which it, in turn, owes obedience. [citations omitted.] In addition, the lower court must implement both the letter and the spirit of the mandate, taking into account the appellate court's opinion and the circumstances it embraces.

Thurston v. Box Elder County, 892 P.2d 1034, 1037-8 (1995). The truth is that this case is over 30 years old; and the record is thousands and thousands of pages long. Nevertheless, this brief can be relatively short because most of the issues have already been decided in *Madsen I* and *Madsen III*.

POINT II
ACCORDING TO THE MANDATE OF THE SUPREME COURT, THERE IS NO STATUTE OF LIMITATIONS FOR THIS CASE

A. BACKGROUND

Madsens took out their home loan in 1964. (Finding of Fact ¶ 1.) (R. 2997. See Ex. D herein.) The complaint in this case was filed on March 3, 1975. (R. 1.) The trial court applied the four-year statute of limitations pursuant to § 78-12-25 (3), *Utah Code Ann.* ("An action may be brought within four years for relief not otherwise provided for by law."). Therefore, the trial court allowed damages from 1975 (date of complaint) back to 1971 (four-year statute of limitations) even though Madsen had been making the same

loan payments since 1964. (R. 2997-8.) Or stated in other words, Prudential was allowed to pocket all of the profits on the pledged funds for the period of 1964 to 1971.

This issue was preserved below at R. 2714-20, 3013-20, 6366, 7610-16, 12744-7.

B. THERE IS NO STATUTE OF LIMITATIONS FOR MONEY "DEPOSITED" IN A BANK

Madsen claims that the applicable statute of limitations should have been § 78-12-34,[4] *Utah Code Ann.* which states:

> To actions brought, to recover money or other property **deposited** with any bank, trust company or savings or loan corporation, association or society **there is no limitation**. (Emphasis added.)

As noted, above, the statute turns on the word "**deposit**." If Madsen's pledged funds were construed to be a "**deposit,**" § 78-12-34 (above) would apply, and damages would go all the way back to 1964. However, Judge Rigtrup rejected plaintiff's claim that the pledged funds were a "deposit." At Conclusion of Law ¶ 9 (R. 3003, Ex. D herein) Judge Rigtrup held that:

> The "budget" account is not a "bank deposit" within the meaning of *Utah Code Ann.* § 78-12-34.

But, the Utah Supreme Court has previously made a ruling on this specific issue. In *Madsen I*, our Supreme Court concluded that Madsen's pledged funds were a "deposit."

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[4] This statute was rescinded in 1981. However, this case was six years old by that time. Thus, the 1981 statute should apply. *See e g. Merz v. Seaman*, 697 N.Y.S.2d 290 (1999) and 51 Am.Jur.2d, *Limitations of Actions*, § 47.

> A deposit[5] of money as security for the performance of a contract has been recognized as a valid pledge.

Madsen I, 558 P.2d at 1339. (Emphasis and footnote added.)

In short, the Utah Supreme Court has determined in this case that Madsen's monthly "pledge" was a "deposit." That mandate is binding on this Court. Since each monthly payment was a "deposit," the statute of limitations regarding "deposit" (§ 78-12-34 above) should apply.

However, if this Court concludes that Madsen's pledge was not a "deposit" (see above), the Court should consider the case of *Conner v. Smith*, 51 Utah 129, 169 P.158, 160 (1917). *Conner* analyzes statute of limitations issues for a "pledge." The *Conner* court held that:

> When property is held by the pledgee as security, he cannot assert that he holds it adversely to the pledgor, and thereby acquire a right to it under the statute of limitations.

C. STANDARD OF REVIEW AND MARSHALING

The standard of review is the one of correctness, because the trial court's application of a statute of limitations presents a question of law. *Estes v. Tibbs*, 1999 UT 52, ¶4, 979 P.2d 823.

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[5]Compare *Hercules Inc. v. Utah State Tax Commission*, 2000 UT App 372, ¶ 9, 21 P.3d 231 ("When a statute fails to define a word, we rely on the dictionary . . .") with *Webster's Third New International Dictionary* (the word deposit defined *inter alia* as "something given as a pledge"). Also the *Oxford American College Dictionary* (2002) defines the word deposit *inter alia* "a sum payable as . . . a pledge for a contract."

Since determining the applicable statute of limitations is purely a legal issue, there is no requirement to marshal evidence. If marshaling is nevertheless appropriate, Prudential may make the factual assertion that the pledge was never deposited into any identifiable account. (R. 2998.) Madsen concedes that fact. Based on this fact, Prudential may argue that the pledge could not be deemed a deposit.

POINT III
ACCORDING TO THE MANDATE OF THE SUPREME COURT, IF ANY STATUTE OF LIMITATIONS APPLIES, IT WOULD BE THE SIX-YEAR STATUTE

A. BACKGROUND

Madsen has argued in POINT II above, that there is no statute of limitations for this case. If the Court agrees with POINT II, the Court may skip this POINT III. However, if this Court disagrees with POINT II, above, the Court should next consider this POINT III.

This issue was preserved at R. 7610-11.

B. IF ANY STATUTE OF LIMITATIONS APPLIES, IT WOULD BE THE SIX-YEAR STATUTE

As noted in POINT II above, Judge Rigtrup applied a four-year statute of limitations pursuant to § 78-12-25(2) *Utah Code Ann.* ("An action . . . for relief not otherwise provided for by law"). However, if any statute of limitations applies (see Point II above), Judge Rigtrup should have applied the six-year statute of limitations. Specifically, § 78-12-23 *Utah Code Ann.* provides:

> An action may be brought within six years . . . upon any contract, obligation, or liability **founded upon an instrument in writing** . . . (Emphasis added.)

The next step is to compare § 78-12-23 (cited above) with the mandate of the Supreme Court in *Madsen I* which states:

> This action is **founded on a deed of trust** and was brought to determine the . . . legal consequences **pursuant to such terms**. (Emphasis added.)

558 P.2d at 1338.

In summary, the mandate of the Supreme Court clearly and specifically holds that "this action" was "founded" on "an instrument in writing" (viz. the trust deed). Thus Judge Rigtrup violated both the letter and the spirit of the mandate by not applying the six-year statute of limitations.

C. STANDARD OF REVIEW AND MARSHALING

The standard of review is one of correctness, because the trial court's application of a statute of limitations present a question of law. *Estes v. Tibbs,* 1999 UT 52, ¶4, 979 P.2d 823.

As stated above, there should be no need to marshal evidence on the legal issue of the applicable statute of limitations. But if marshaling is required, Prudential may argue that there is nothing in the contract which explicitly requires Prudential to pay the interest, earnings, or profits it derived from the pledge. (R. 152.) Prudential may go on to argue that there was, therefore, no contractual breach.

POINT IV
ACCORDING TO THE MANDATE OF THE SUPREME COURT, IT WAS AN ERROR OF LAW FOR THE TRIAL COURT TO END DAMAGES AS OF 1979

A. BACKGROUND

Madsens took out their home loan in 1964. The duration of the loan was for 25 years (or until 1989). This lawsuit was filed in 1975. Or stated in other words, this lawsuit seeks damages for the period of 1964 to 1989.

However, the trial court cut off damages for the period from 1964 to 1971. See Points II and III above. The trial court also cut off damages for the period 1979 to 1989. This Point IV deals with damages from 1979 to 1989.

In 1979 (two years after the Court's decision in *Madsen I*) the Utah Legislature passed a new statute titled the *Interest on Mortgage Loan Accounts Act* (§ 7-17-1 *et seq.* U.C.A.) There have been some amendments since the original 1979 act. A copy of the act as amended by 1985 (the date of the trial below) is included as Exhibit J.

Section 4 of the original act states as follows:

> (1) A lender not requiring the establishment and maintenance of a reserve account shall offer the borrower the following options:
>
> (a) The borrower may elect to maintain a non-interest-bearing reserve account[6] to be serviced by the lender at no charge to the borrower; or

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[6] § 7-17-2(5) defines "reserve account" as follows: "'Reserve account' means any account, whether denominated . . . pledge . . . or otherwise . . . whereby the borrower agrees to make periodic prepayment to the lender . . [of] taxes, insurance premiums or other charges . . ."

(b) The borrower may manage the payment of insurance premiums, taxes and other charges for his own account.

Pursuant to the above statute, Prudential sent a form letter to Madsen and other class members in July of 1979. That form letter states:

NOTICE TO HOMEOWNER
RESERVE ACCOUNTS FOR PAYMENT OF TAXES AND INSURANCE

As of July 1, 1979, Prudential Federal Savings will no longer require a reserve account in conjunction with your mortgage loan for the payment of real estate property taxes, insurance premiums, or other charges. You may now choose one of the following two options:

A. You may continue your monthly payment as is now provided for in your loan documents to be deposited in a non interest bearing reserve account. We will continue to provide you the service of paying your property taxes and/or insurance premiums at no cost as they become due; or,

B. You may elect to assume the legal responsibility for the payment of these assessments and pay your own real estate property taxes, insurance premiums and other charges as they become due.

If you choose Option A, no response is necessary. We will continue to provide the services of paying these assessments without cost to you. If you choose Option B, the enclosed card must be signed and returned to our office by September 1, 1979.

(R. 3007.) (Emphasis added.)

In summary, based upon the letter (above) and based upon § 7-17-4 (above) Judge Rigtrup cut off damages as of July of 1979 even though Madsen and other class members continued to pay pledged funds for several years after 1979. Thus Conclusion of Law ¶ 5 states:

> Damages terminate on June 30, 1979 by reason of *Utah Code Ann.* § 7-17-4. (R. 3002, Ex. D herein)

This issue was preserved, *inter alia*, at R. 6872-76, 6975-84, 7258-64, 9104-12, 10838-48.

B. BY ITS OWN TERMS, THE STATUTE DOES NOT APPLY TO THE INSTANT LAWSUIT.

As described above, the legislature passed a new statute in 1979 (Interest on Mortgage Loan Accounts Act). Based upon § 7-17-4 of that Act, Judge Rigtrup cut off damages as of 1979. (See Conclusion of Law ¶ 5, R. 3002.) However, § 7-17-10 of the Act states:

> **The provisions of this act shall apply:**
> (1) to all reserve accounts; and
> **(2) to all actions filed after January 1, 1979, to recover interest on or other compensation for the use of the funds on any reserve account whether or not the reserve accounts were established prior to or subsequent to July 1, 1979.** (Emphasis added.)

Thus, according to the specific language of the statute (above), the act only applies to actions filed **after** January 1, 1979. But, the instant lawsuit was filed in 1975, four years prior to that 1979 deadline. Thus, the act cannot apply. See *Andreason v Felsted*, 2006 UT App 188, ¶11, 137 P.3d 1:

> When we engage in statutory interpretation, "we are compelled to give the statutory language meaning and to assume that each term in the statute was used advisedly." (Citation omitted.)

The case of *Nelson v. Salt Lake County*, 905 P.2d 872, 876 (Utah 1995) is also on point:

> Clearly, the first and last sentences of [the statute] are patently inconsistent. . . . This Court will not construe a statute in such a way as to render certain viable parts meaningless and void.

If this Court goes beyond the plain words of the statute to examine the legislative history,[7] the court will be squarely faced with the comments of the sponsor of the bill:

> It is very clear and this has been established in the Senate and the argument is without doubt that the Madsen case is not included in this . . . The Madsen suit is not encumbered in any way. It can go ahead with logical conclusion. We don't wish to interfere with that.

Legislative Proceedings on Senate Bill 85, Vol. II, 2/14/79, p.19. (R. 3271-2.)

In summary, Madsen's rights to damages after 1979 could not be cut off by § 7-17-4 *Utah Code Ann.* because that statute only applies to **"actions filed after June 1, 1979."** But, this lawsuit was filed in 1975.

C. PRUDENTIAL CANNOT RELY ON THE STATUTE BECAUSE PRUDENTIAL DID NOT DEPOSIT MADSEN'S PAYMENTS INTO A "NON-INTEREST BEARING" ACCOUNT

Turning again to the letter sent by Prudential to Madsen and other class members (R. 3007, ¶ A above), the letter reads in part:

> You may continue your monthly payment as is now provided for in your loan document to be deposited in a noninterest bearing account. (Emphasis added.)

But, did Prudential really "deposit" the money "in a non-interest bearing account" as promised by Prudential's letter? The analysis begins with Judge Rigtrup's Finding of Fact ¶ 5, which states that:

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[7] See *Utah Dept of Environmental Quality v Wind River Petroleum*, 881 P.2d 869, 872-3 (Utah 1994).

> Upon receiving each monthly payment, Prudential immediately deposited the entire check into its general operating account. (R. 2998.) (Emphasis added.) (See Ex. D.)

Madsen hired an expert witness, Andrew Carr Conway. Mr. Conway has impeccable credentials. He is a Certified Fraud Examiner, a Certified Financial Investigator, and a Certified Public Accountant. (See R. 11883-4.) Mr. Conway has had thirty years of experience with the Securities and Exchange Commission and the Internal Revenue Service. Mr. Conway's testimony[8] on the issue is as follows:

> I have examined a form letter which was sent by Prudential in July of 1979 to persons who had borrowed money from Prudential to purchase homes (class members). . . . I have also examined a document titled *Findings of Fact and Conclusions of Law* (March 22, 1990).
>
> * * *
>
> Based on the above documents and my review of the 1990 Annual Report for Olympus Capital Corporation (a consolidated entity including Prudential), it is my opinion, as a cash management issue, and as an accounting matter related to the classification of restricted cash, **Prudential did not deposit the funds designated for taxes and insurance with Madsen's monthly payments into a "non-interest bearing reserve account"** after July 1, 1979 (as promised in the July 1979 letter). Rather, (contrary to the representations in the 1979 form letter,) after July 1, 1979, until at least May 22, 1990 (the date that Findings of Fact and Conclusions of Law were signed) **Prudential deposited Madsen's monthly "budget payment" into Prudential's general operating account and Prudential invested surplus funds from the general operating account at a profit.** (R. 11876-9.) (Emphasis added.)

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[8] Prudential filed a Motion to Strike the Conway Affidavit. In response, Judge Dever ruled that "Mr. Conway's statements on accounting procedures [are] allowed, the remaining portions in the Affidavit and Supplemental Affidavit are striken. (R. 12771.)

The summary of all the above is that Prudential's form letter (¶ A above) promised to "deposit" the prepayments for taxes and insurance into a "non-interest bearing account." But that was a lie. Prudential did not deposit the money into a "non-interest bearing account." Rather, Prudential deposited the money in its "general operating account," and Prudential invested surplus funds from this account to earn a profit. *See* Conway Affidavit above. *See also* Finding of Fact ¶ 9 (R. 2999, Ex. D. herein).

It is also important to note that the statute required Prudential to advise class members that the form letter was sent out "pursuant to this Act." [viz. pursuant to § 7-17-4(2).] Of course, Prudential's form letter does not advise class members that the letter was sent "pursuant" to § 7-17-1 *et seq*. (See ¶ A above.) Therefore, class members did not have any opportunity to refer to the statute in order to clarify any ambiguity.

D. STANDARD OF REVIEW AND MARSHALING

The interpretation of a statute is a question of law which the appellate court should review for correctness. *N.A.R., Inc. v. Elmer*, 2006 UT App 293, ¶4, 141 P.3d 606.

The only factual issue may involve Conway's statement (above) that Prudential did not deposit the pledge into a non-interest bearing account. However, there is no contrary fact evidence to marshal. Prudential merely argued that Conway's affidavit should not be considered because of technical considerations, for example, that it contained legal conclusions. R. 12014. Prudential went on to assert that the affidavit was irrelevant, in

that it addressed "Prudential's *internal* accounting procedures." R. 12023. Prudential thus acknowledged that this statement does not present a relevant factual issue.

POINT V
ACCORDING TO THE MANDATE OF THE SUPREME COURT, PRUDENTIAL MUST PAY PRE-JUDGMENT INTEREST

A. BACKGROUND

The Master computed the "net" profits which Prudential had realized by investing Madsen's pledged funds. The trial court awarded Madsen those cumulative earnings for the years 1971 to 1979. However, the trial court refused to grant any prejudgment interest on those amounts. (See Conclusions of Law, ¶¶ 10 and 13, R. 3003, at Ex. D. herein.)

This issue is preserved at R. 3034-43, 6456-7, 7982-3, 12229-35, 12700.

B. TRIAL COURT RULINGS

Judge Rigtrup awarded prejudgment interest of ten percent on the damage award from the date of the trial (1985) to the date of the entry of judgment (2006) (R 3003, Ex. D herein at ¶ 13) However, Judge Rigtrup refused to grant any prejudgment interest for the years prior to 1985 because:

> Plaintiffs shall not be allowed interest for any time prior to trial, for the reasons that the damages were not calculable before trial, that damage calculation at trial was subject to divergent evidence and viewpoints, especially between the parties' expert witnesses, that damages required a determination by the Court and that the Court was required to select one method of calculation from among several alternatives presented by the experts.

R. 3003-4, Exhibit D herein at ¶ 13.

However, at a much later date, Judge Stirba ruled that:

> Judge Rigtrup's award to plaintiffs of the simple interest at the annual rate of 10% on damages from the date of the conclusion of trial but prior to the entry of judgment, is hereby vacated on the ground a judgment is entered when the judgment is actually signed and entered, and an award of prejudgment [interest] is, therefore, inappropriate.

Order of January 20, 1998 (R. 6794, Ex. F).

In summary, based upon the rulings of Judge Rigtrup and Judge Stirba, no prejudgment interest was awarded.

C. ARGUMENT

The law on prejudgment interest has been stated as follows:

> A prejudgment interest award is proper when "the damage is complete, the loss can be measured by facts and figures, and the amount of the loss is fixed as of a particular time."

Lefavi v. Bertoch, 2000 Utah App. 5, ¶ 24, 994 P.2d 817, 823. (Emphasis added.)

Turning now to the mandate of the Supreme Court, in this very case, we find the following language:

>]I]t [is] of no consequence that the amount of [Madsen's pledge] may vary during the existence of the pledge. The amount is ascertainable at any given time, and thus the lien is perfected as to amount.

Madsen I at 1339. (Emphasis added.)

Or, stated in other words, the Supreme Court has concluded in this very case that the amount of the pledge is "ascertainable at any given time." See *Madsen I.* Since the amount of the pledge is "ascertainable at any given time," the *Lefavi* test (above) is satisfied, and prejudgment interest should be awarded.

D. STANDARD OF REVIEW AND MARSHALING

"A trial court's decision to grant or deny prejudgment interest presents a question of law which we [the appellate court] review for correctness. *Carlson Distributing Co v. Salt Lake Brewing Co. L.C.,* 2004 UT App 227, ¶15, 15 P.3d 1171.

An issue of law needs no marshaling. But should marshaling be appropriate, Prudential would probably rely on Judge Rigtrup's factual characterization (see quote on p. 19). [9]

POINT VI
ACCORDING TO THE MANDATE OF THE SUPREME COURT DAMAGES SHOULD BE COMPOUNDED AND THE COMPOUNDING SHOULD CONTINUE TO THE PRESENT DAY

A. BACKGROUND

The trial court allowed damages from 1971 to 1979.[10] During this window of 1971 to 1979, the trial court computed separate damages for each year, and the Court compounded the interest each year from 1971 to 1979. No compound interest was allowed after 1979. (See Findings of Fact and Conclusions of Law at Ex. D herein.)

This issue is preserved at R. 6457-9.

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[9] However, Judge Rigtrup incorrectly applied the law to these facts. See *Smith v. Fairfax Realty*, 2003 UT 41, 82 P.3d 1064 ("Where, as here, damages were complete as of the day the property was transferred to the REIT and the jury based its award of damages on competent testimony from an appraiser who used generally accepted principles in determining the market value of the real property, an award of prejudgment interest is appropriate.")

[10] Madsen has argued in Point II and III above that the trial court should have allowed damages prior to 1971 and Madsen has argued in Point IV, above, that the trial court should have allowed damages after 1979.

B. THE TRIAL COURT WAS CORRECT IN COMPOUNDING DAMAGES FROM 1971 TO 1979

According to the mandate of the Supreme Court in this case:

> [T]he secured party may hold as additional security any increase or profits (except money) received from the collaterals, but money so received, unless remitted to the debtor, shall be applied in reduction of the secured obligation . . .

Madsen I at 1340. (Emphasis added.)

But Prudential violated the mandate of the Utah Supreme Court by failing to apply profits from the pledged funds "in reduction of the secured obligation."

In short, Prudential earned a double profit from Madsen's pledged funds. First Prudential earned a "profit" by investing Madsen's pledged funds. But Prudential earned a second profit by failing to reduce the overall loan balance by the profits earned on Madsen's pledged funds. Since Prudential was earning a double profit on Madsen's pledged funds, the remedy is to award Madsen compound interest. Thus, in Finding of Fact ¶ 14, the trial court ruled:

> The Court finds it appropriate under the facts of this case to compound on an annual basis. The Court finds that Prudential must disgorge these compounded profits in order to make Madsen whole. (R. 2999.)

The case of *Farnsworth v. Farnsworth*, 117 Utah 494, 217 P.2d 571, 577 (1950) is in accord. The *Farnsworth* court stated:

> If defendants had paid plaintiff the interest when due, he could have reloaned it to them, or could have loaned it to any one else . . . *The plaintiff therefore was as much entitled to interest upon the unpaid interest as though it had been paid to him when due and he had reloaned it* . . . (Emphasis in original.)

Comment 207(2) to the Restatement of Trusts (1959) leads to a similar result:

> If the trustee uses trust funds in his own business and it does not appear how much he has earned thereon, he is ordinarily chargeable with compound interest on the ground that he probably received a return from the trust fund so used at least equal to compound interest.

C. COMPOUND INTEREST SHOULD ALSO BE AWARDED FOR THE YEARS 1964 TO 1971

Madsen has argued in Point II above that damages should also have been awarded from 1964 to 1971. For reasons stated, above, any damages awarded from 1964 to 1971 should likewise be compounded.

D. COMPOUND INTEREST SHOULD ALSO BE AWARDED FOR YEARS AFTER 1979

Madsen has argued in Point IV above that damages should also have been awarded after 1979. For reasons stated above, any damages awarded after 1979 should likewise be compounded.

E. COMPOUNDING OF OLD DAMAGES SHOULD CONTINUE AFTER 1979 EVEN IF THE COURT DOES NOT AWARD NEW DAMAGES AFTER 1979

According to the trial court, Prudential owed Madsen $134.70 as of 1979. But according to the trial court, Prudential still owes Madsen the same $134.70 as of 2006. The problem is that the trial court has not followed the mandate of the Supreme Court.

According to the Supreme Court, Prudential should have reduced Madsen's mortgage balance by $134.70 as of 1979. (See ¶ B above.) Of course, if Madsen's mortgage balance had been reduced by $134.70 in 1979, the loan would have been paid

off earlier and Madsen's interest payments after 1979 would have been less. Or stated in other words, Prudential has continued to earn profits on Madsen's $134.70 from 1979 to 2006. But according to the mandate of the Supreme Court, profits earned on the $134.70 belong to Madsen. The only remedy is to allow the interest on the $134.70 to compound each year from 1979 until the judgment is paid.

F. STANDARD OF REVIEW AND MARSHALING

Issues regarding interest are conclusions of law which should be reviewed for correctness. No particular deference should be paid to the trial court rulings. *Christensen v. Munns*, 812 P.2d 69 (Utah App. 1991).

Issues of law do not require marshaling. If marshaling is appropriate, the only fact issue would seem to be whether Prudential has ever reduced Madsen's loan balance by the annual earnings on the pledged funds. (See p. 22 above.) Madsen is aware of no facts to support such a contention.

POINT VII
ACCORDING TO THE MANDATE OF THE SUPREME COURT THE TRIAL COURT ERRED BY REMOVING DUPLEXES, SECOND HOMES, COMMERCIAL PROPERTIES, ETC. FROM THE CLASS

A. BACKGROUND

On June 14, 1977, Judge Croft certified a class consisting of

> [A]ll persons who are presently parties to trust deed contracts with defendant wherein the contract provides that:
>
> * * *
>
> "In addition to the monthly payments as provided in said note, the trustor agrees to pay to the beneficiary, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted

> from time to time as required, and said budget payments are hereby pledged to the beneficiary as additional security for the full performance of this deed of trust and the note secured thereby. . . ." (R. 640.) (Emphasis added.)

On September 3, 1985, Judge Rigtrup reconfirmed Judge Croft's class certification order above. Specifically, Judge Rigtrup ruled that:

> [T]he memorandum decision of Judge Croft dated June 14, 1977, is hereby reconfirmed. (R. 2027.)

However, in December 1996, Judge Rigtrup narrowed the class definition. Specifically, the Court stated:

> The Court will certify as to class . . . single family, owner- occupied residential primary residence borrowers . . . (R. 5522.)

According to Judge Rigtrup's 1996 revision, duplexes, tri-plexes, second homes (or cabins) and corporate owned homes were excluded.

Judge Rigtrup's rationale for narrowing the class (as described above) was that:

> My reasoning between the non-occupied or commercial kinds of loans is where they are either holding rental property or apartments or commercial kinds of loans, they may have an interest to go back and borrow more money. And so they'd be concerned with the relationship with Prudential in terms of being able to go back to in the well. A homeowner probably isn't really going to consider it because you are trying to get the best deal you can and buy yourself a home. (R. 5523.)

This issue is preserved at R. 5026-31, 5210-15.

B. THERE IS NO CASELAW TO SUPPORT JUDGE RIGTRUP'S NARROWING OF THE CLASS

Neither Judge Rigtrup nor Prudential has ever cited a single case which holds that a court can exclude some parties from a class on the guess that they might not want to be

part of the class action. To the contrary, see e.g. *Lanner v. Wimmer*, 662 F.2d 1349, 1357 (10th Cir. 1981): "It is not fatal if some members of the class might prefer not to have violations of their rights remedied." (Internal quotations omitted.)

C. ACCORDING TO THE MANDATE OF THE SUPREME COURT, OWNERS OF DUPLEXES, SECOND HOMES AND COMMERCIAL PROPERTIES SHOULD BE PART OF THE CLASS BECAUSE THEY SIGNED IDENTICAL CONTRACTS.

Again, the answer to this question is found by turning to the mandate of the Utah Supreme Court. According to that mandate:

> The action is **founded upon terms of a deed of trust**; and was brought to determine the status of the parties, and **the legal consequences pursuant to such terms**. (Emphasis added.)

Madsen I, 558 P.2d at 1338.

And according to the mandate of the Supreme Court, the "legal consequences" of the Madsen contract are as follows:

> If from the use of the property pledged profits are derived, the **pledgee [Prudential] must . . . account therefor to the pledgor**. (Emphasis added.)

Id., 558 P.2d at 1340.

The point is that the Utah Supreme Court has now issued a mandate which has construed the terms of a **specific** contract; and approximately 10,000 Utah citizens had an **identical** contract with Prudential. According to the above mandate **Prudential must account to each pledgor if the pledgor has a contract identical to the Madsen contract**. In summary, Judge Rigtrup failed to follow the mandate of the Utah Supreme

Court when he excluded duplexes and other commercial properties from the class – even though they had signed **identical** contracts.

As a final matter, Rule 23(e) U.R.C.P provides that:

> A class action shall not be dismissed or compromised without approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs. (Emphasis added.)

The above Rule ties in with Rule 23(c)(4)(B), which states:

> When appropriate . . . a class may be divided into subclasses and each subclass treated as a class.

In effect, Judge Rigtrup created a separate subclass of homeowners who lived in duplexes, or other commercial properties. Then, twenty years after the class was certified, Judge Rigtrup dismissed the entire subclass without sending the notice required by Rule 23(e) (above).

Suppose that a duplex owner had received a letter from the court explaining that duplexes had been dismissed from the class. At that point the duplex owner could have filed a separate and independent action to collect or the duplex owner might have filed a motion to intervene. But, because there was no notice from the court, duplex owners had no opportunity to protect themselves.

D. STANDARD OF REVIEW AND MARSHALING

Whether the trial court applied the correct legal standard in reaching its decision on class certification is a legal question reviewed de novo. *Parker v Time Warner Entertainment Co* , 331 F.3d 13, 18 (2d Cir. 2003).

There is no need to marshal evidence pertaining to a legal issue. However, should marshaling need to be addressed, there is no evidence in the record supporting the factual basis Judge Rigtrup gave (see ¶ A above) for his decision to narrow the class.

POINT VIII
THE MASTER SHOULD BE DISQUALIFIED AND ALL OF HIS WORK VACATED

A. BACKGROUND

The trial, conducted by Judge Rigtrup, computed damages only for Madsens, individually. (Findings of Fact and Conclusions of Law at Preamble and Conclusion ¶ 12, R. 2994, 3003.) (See Ex. D. herein.) After the trial was completed, the trial court appointed a Special Master. The job of the Master was to compute damages for all class members. Over a period of approximately ten years, the Master issued various preliminary reports. (R. 4068-71, 5384-7, 9339-55.) The Master's final report was issued on March 1, 2002 (R10370-72 and Ex. G herein); and the Final Judgment was based entirely[11] on that March 1, 2002 Report.

This issue was preserved at R. 9645-51, 10462-4.

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[11] The Final Judgment entered on December 13, 2004 states in part: "[P]ursuant to the Master's Fifth Report . . . judgment is entered . . . in the amount of $1,004,153.00 . . ." (R. 13429.) (Emphasis added.) cf. Final Judgment, entered June 1, 2006. (R. 13842. See Ex. I.)

B. THE MASTER SECRETLY GAVE HIS REPORT TO PRUDENTIAL BEFORE THE REPORT WAS GIVEN TO MADSEN OR THE COURT

James Loebbecke was a member of the Board of Directors of Prudential (then Olympus Bank) up until 1985. After 1985, James Loebbecke became the designated expert witness for Prudential. (R. 8533, 8635, 8687.)

In the course of discovery it became apparent that Mr. Loebbecke was involved in at least three *ex parte* meetings with the Master (Ed Erickson). (R. 9657-63.)

Several courts have disqualified a Master based upon such *ex parte* meetings. See e.g. *Plumb v State*, 809 P.2d 734 (Utah 1990); *Cobell v Norton*, 334 F.3d 1128 (D.C. Cir. 2003); and *Jenkins v Sterlacci*, 849 F.2d 627, 632 (D.C. Cir. 1988).

But the instant case is much stronger than *Plumb*, *Cobell* and *Jenkins*, and other similar *ex parte* cases. In *Plumb*, *Cobell*, and *Jenkins*, we simply know that *ex parte* meetings were held; however, nothing is known about what happened at those *ex parte* meetings. But, in the instant case, we know what happened during the *ex parte* meeting between the Master (Ed Erickson) and James Loebbecke (Prudential's expert witness). Specifically, we know that the Master (Ed Erickson) made a private deal to show his report to James Loebbecke (Prudential's expert witness) before the report was given to Madsen's attorney or the Judge. After one of those *ex parte* meetings, Mr. Loebbecke made the following hand written notes:

> Ed [Erickson - The Master] will draft his findings for a meeting with attorneys. Will share with me first.
> (Emphasis added.) (R. 9672.)

Why would the Master show his report to Prudential's expert witness (Loebbecke) before he showed the report to Madsen's attorney or to the Judge? Was the Master doing a special favor for Prudential? Did the Master have special friends at Prudential? Did Prudential make some secret promises to the Master? Of course, no one will ever know. But the public can have no confidence in such secret meetings and private deals between Prudential and the Master.

The above conduct also squarely violates Rule 53(e)(5), *Utah Rules of Civil Procedure* which states:

> Before filing his report a master may submit a draft thereof to counsel for all parties [not the expert witness for one of the parties] for the purpose of receiving their suggestions. (Emphasis added.)

C. THE MASTER HAS NEVER EVEN SEEN THE BASIC DOCUMENTS WHICH FORM THE FOUNDATION FOR HIS REPORT AND THE FOUNDATION FOR THE FINAL JUDGMENT

On January 2, 2002, the Court entered the following Order:

> The Master shall, within 60 days of this order, produce to the Court a report giving the Master's final statistical calculation of aggregate class damages. (R. 10201.)

Pursuant to the above Order, the Master sent the following Report[12] to the Court on March 1, 2002.

> This letter is our Report to the Court as required by the Court in its Order dated January 2, 2002.
>
> * * *
>
> To accomplish this objective I met with Brad Slack at Washington Mutual to review the data base that he had prepared of

[12] This entire Report of March 1, 2002 is included herein as Ex. G.

> the loan origination cards. This data base was prepared by Mr. Slack and other Washington Mutual Bank employees under his direction, as outlined in his August 7, 2000 affidavit filed with the Court. This process resulted in a data base of 14,482 loan cards. (R. 10370.) (Emphasis added.)

As described in the Master's March 1, 2002 Report (above), the Master did not do the work to create the database of 14,482 loan cards. Rather, the work was done exclusively by employees of Prudential (Brad Slack). The August 7, 2000 Affidavit of Brad Slack (discussed above) explained how he (Brad Slack) created the database of 14,482 cards.

> I physically sorted through over 70,000 loan origination cards and identified over 10,000 loan cards reflecting loans that may be within the class defined in this action. This process took over 600 hours (R. 8493.)

Finally, it is crucial to note the Master's Final Report of March 1, 2002 (R. 10370, Ex. G) states:

> I [Ed Erickson, the Master] have not yet performed testing to determine if all [70,000] loan cards have been properly segregated between class members and non-members of the class. (Emphasis added.)

In summary, the Master has never seen the 70,000 loan cards and has never done testing to determine how many class members were in that pool of 70,000 loan cards. The only person who has ever seen the 70,000 loan cards is Brad Slack, an employee of Prudential. A Final Judgment should not be based upon the work of Prudential employees which has never been seen or tested by the Master.

D. THE MASTER'S CLAIM THAT HE HAD DONE A "LIMITED AMOUNT OF TESTING" WAS INCORRECT

As described in ¶ C above, the Master has never seen or tested the original pool of 70,000 loan cards. Rather, it was a Prudential employee (Brad Slack) who sorted the 70,000 loan origination cards to end up with a "data base" of 14,482 class members.

However, the Master did claim that he had done "a limited amount of testing" of the "data base" of 14,482. Thus, the Master's Final Report of March 1, 2002 (R. 10370, Ex. G) states:

> It should be noted that I have only performed a limited amount of testing of this data base [14,482 loan cards], primarily in obtaining a sample of 50 loan cards to respond to plaintiff counsel's request of December 27, 2000. (Emphasis added.)

In order to evaluate this claim (viz. "I have . . . performed a limited amount of testing.") Madsen employed Andrew Carr Conway, Sr. Mr. Conway is a Certified Public Accountant, a Certified Fraud Examiner, and a Certified Financial Investigator. Mr. Conway's experience includes thirty years with the Internal Revenue Service and the Securities Exchange Commission. Mr. Conway gave a total of four affidavits on various issues in the case. (R. 11862-84, 12156-62; 12468-72; and 12605-13.) However, the Conway affidavit of September 25, 2003 analyzes the Master's claim that:

> I have only performed a limited amount of testing of this data base, primarily in obtaining a sample of 50 loan cards to respond to plaintiff counsel's request of December 27, 2000. (R. 10370.) (See above.)

Mr. Conway has given the following testimony[13] in response to the claim of "a limited amount of testing."

> That process of picking up and delivering cards is best described as an "errand boy." There is absolutely no basis in the accounting profession to label that process as "testing" sufficient to produce sufficient relevant data. First of all, a sample of 50 cards from a universe of 70,000 cards is <u>much</u> too small a sample to do any legitimate testing. But if the Master wanted to attempt some type of testing, he would have applied examination procedures, including the application of certain mathematical formulas, either to produce his own statistical calculation or to test Prudential's calculations, to those 50 cards. The report dated March 1, 2002 does not include any evidence that the Master performed any examination procedures including the application of mathematical computations to the 50 card sample. Indeed there is no evidence, based on the Report, that *the Master even read the cards.*
>
> * * *
>
> In summary, it was deceitful for the Master to <u>pretend</u> that he had done a "limited amount of testing" when there was in reality no statistical "testing" of any kind, based on his Report dated March 1, 2002 and the related historical record in the case. (Emphasis from original.)

<u>E. THE MASTER HAS ADMITTED THAT HIS MARCH 1, 2002 REPORT WHICH FORMS THE BASIS FOR THE FINAL JUDGMENT IS NOT YET FINISHED</u>

As noted in ¶ A, above, the <u>Final Judgment</u> in this case is based entirely on the Master's Report of March 1, 2002. (See Ex. G herein.) However, the Master, himself, has acknowledged that his March 1, 2002 report is not yet finished.

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[13] Prudential filed a <u>Motion to Strike the Conway Affidavit</u>. In response, Judge Dever ruled that "Mr. Conway's statements on accounting procedures [are] allowed, the remaining portions in the Affidavits and Supplemental Affidavit are stricken. (R. 12771.) Prudential did <u>not</u> file a counter-affidavit.

On September 12, 2003, the Master wrote a letter to Judge Dever (R. 12760-62, included as Ex. H herein). As part of that letter, the Master stated:

> I was careful to point out, both on page 1 and page 3 of my Report, that the **loan data base had not been extensively tested.**
>
> * * *
>
> As I stated in my letter to Mr. DeBry of April 23, 2003 . . . "**of course, as this matter progresses to the point where damages are distributed to class members, we will perform additional testing to confirm proper identification of class members and completeness of the data base."**
>
> * * *
>
> **I have consistently stated . . . that only a limited amount of testing had been done and more testing would be required!** (Emphasis added.)

Obviously, a Final Judgment should not be based upon a Master's Report which states that **more testing would be required**. Or stated in other words, the Final Judgment should only be entered after all of the testing is done.

F. THE MASTER'S FINAL REPORT IS DEFECTIVE BECAUSE IT DID NOT INCLUDE "EVIDENCE" OR "EXHIBITS"

As described in ¶¶ C and D above, a major defect in the Master's Final Report is that the Master has never seen the 70,000 loan origination cards which form the foundation of this entire case. But, all of that confusion and delay could have been avoided if the 70,000 loan cards had been filed with the Court as required by Rule 53(e)(1), U.R.C.P. which states:

> The master shall prepare a report upon the matters submitted to him by the order of reference . . . He shall file the report with the clerk of the court and in an action to be tried without a jury, unless otherwise directed by the order of reference, shall file with it a transcript of the proceeding and of the evidence and the original exhibits. (Emphasis added.)

However, in violation of Rule 53(e)(1) (above) the Master's Final Report of March 1, 2002 (Exhibit G) did not include any "evidence" or any "exhibits." Rather, the Final Report of March 1, 2002 simply contains three pages of conclusions. (R. 10370-2.)

Because of the failure to file "exhibits" or "evidence," plaintiffs filed a Motion that the Master Complete the Report of March 1, 2002 (R. 10572.) The above motion requested copies of specific documents which the Master had used in performing his calculations as per the March 1, 2002 report.

In response to plaintiff's motion (above) Judge Dever ruled on January 23, 2004 that:

> The Master's report is complete. The Order signed by the Court directed the Master to provide a "Final statistical calculation of the aggregate class damages." (Order January 2, 2002.) The Master has done this. (R. 10371.)
>
> The Rule does not require that the Master file with the Court each and every documents used in the statistical plan submitted to the Court. It is the statistical plan that is the critical item and that has been accepted by the court. [Madsens'] Motion is denied. (R. 12766.)

According to Judge Dever's ruling (above): "It is the statistical plan that is the critical item." But statistical plans are based upon raw data. And, that data exists on pieces of paper (or microfilm or microchips). According to Judge Dever's ruling, 50,000 Utah citizens will be bound by the Master's "statistical plan"; but no one should be allowed to see the pieces of paper that contain the raw data which formed the basis for the "statistical plan."

However, Rule 53(e)(1) (above) does not give the trial court any discretion. Rule 53(e)(1) is clear and mandatory ("shall file . . . evidence . . . and exhibits"). (Emphasis added.)

The reasoning behind the rule (filing of exhibits) is explained in the federal case of *Shafer v. Army & Air Force Exchange Service*, 277 F.3d 788, 790 (5th Cir. 2002):

> The Federal Rules of Civil Procedure provide that in non-jury actions such as this one, "the court shall accept the master's findings of fact unless clearly erroneous." Fed.R.Civ.P. 53(e)(2). We interpret this rule as imposing an independent obligation on the district court to review the Special Master's factual findings for clear error. . . . This duty includes examining all relevant evidence, including in some cases the hearing transcripts in their entirety. (Emphasis added.)

Obviously, in the case at bar, the trial court was not able to **"examine all relevant evidence"** because no evidence and no documents were filed with the Master's March 1, 2002 Report.

G. STANDARD OF REVIEW AND MARSHALING

The standard of review is whether the trial court abused its discretion (perhaps as a matter of law) in refusing to disqualify the Master and in adopting the Master's report. *Plumb v. State*, 809 P.2d 734, 742-3 (Utah 1990). If there was abuse of discretion, this Court "must vacate the order unless the error was harmless." *Id.* at 741. "The standard for determining harmless error is whether it is reasonably likely that the trial court's final order would have been different absent the master's improper activities." *Id.* at 744.

There appears to be no evidence contradicting the basic facts set forth above, including the *ex parte* contacts. These primary facts are admitted by the Master.

Likewise, there is no evidence contradicting Mr. Conway's more conclusory facts. As reviewed on page 18 above, Prudential merely argued that Mr. Conway's affidavit contained legal conclusions or irrelevant facts.

Although there appears to be no contrary factual evidence, the Master did give reasons for his *ex parte* contacts and for his failure to do statistically significant testing.

As to *ex parte* contacts, the Master wrote the following in his letter to Judge Burton dated September 26, 2001 (R. 9700-03):

> At a meeting with counsel of both plaintiff and defendant present, it was proposed and agreed that the Master would test the sample of 400 borrowers previously conducted by Prudential personnel . . . My recollection is that we discussed the fact this would require us to meet with Prudential's representatives . . . (R. 9700.)
>
> Throughout my CPA career, anytime I have tested work performed by others it has always been my practice to discuss with those who performed the work any exceptions I believe I have found. I have found this to be absolutely necessary since, on occasion, I or my staff may believe we have identified an error or exception, but after obtaining additional information based on discussions with the parties involved it becomes clear that no exception or error had occurred. Since this has been my practice, I assume that Mr. Loebbecke's notes referring to me discussing a draft of my findings with him first would relate to this process of reviewing and confirming any potential exceptions noted in Prudential's work. (R. 9701.)

Prudential would argue that this shows that the *ex parte* contact was not wrong, but only standard procedure

Regarding the Master's failure to do statistically significant testing, the Master wrote the following in his letter to Judge Burton dated March 20, 2002 (R. 10484-6):

> I will reiterate that my firm did test the sample work performed by Washington Mutual, as described in my December 31, 1996 report to the Court. We tested 20 of the 400 sample records and found two minor exceptions, as noted in our December 31, 1996 report. . . . This had a small impact on the interest portion of the calculation but no affect on the damage portion. The other error noted in our testing resulted in a $6.44 difference . . . (R. 10484.)
>
> [S]amples cannot, by definition, produce an exact answer. An exact answer can only be obtained when sampling is set aside and all records are categorized. . . . The actual number is 98.95 % of the sample estimate. If nothing else, this provides additional evidence validating the sampling process. (R. 10485.)
>
> As indicated above, we did test the 1993 sample performed by Washington Mutual and arrived at our own independent computations. (R. 10486.)

Prudential would argue that this shows that the Master was only supposed to do sampling. There was no requirement that there be enough samples for the testing to be statistically significant.[14]

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[14] However, Prudential has never come forward with any factual evidence to show what size sample is needed to produce statistically significant results. For example, Prudential supposedly tested 400 records from a universe of 17,000 records. (R. 5385) The Master was not present and did not participate in the testing of the 400 records. Prudential has never offered evidence that testing of 400 from a universe of 17,000 is statistically significant. But worse still, the Master did not start again to do his own independent test of 400 different records. Rather, the Master tested 20 out of the Prudential's sample of 400 – which in reality means the Master independently tested 20 files from a universe of 17,000 files. Prudential has never offered evidence to show that a sample of 20 from a universe of 17,000 can be statistically significant.

(R 10484.)

POINT IX
THIS CASE CAN COME TO A SPEEDY CONCLUSION

A. THIS CASE WILL NEED TO BE REMANDED

For all of the following reasons, this case should be remanded for further proceedings in the trial court:

A. Damages should be computed for the years prior to 1971. (See Point II above.)

B. Damages should be computed for the years after 1979. (See Point IV above.)

C. The Master's work was not completed. (See Point VIII, ¶ D above.)

D. The Master should be replaced. (See Point VIII, ¶ B above.)

The trouble with all of the above is that this case is now **thirty-two years old.** Because of this specific problem, on October 28, 1996, Madsen filed a Motion that Master Perform an Auxiliary Computation of Damages . . . (R. 5035-7) (included herein as Ex. E.) The computation was to be at Madsen's expense. Of course, the purpose of the motion was so that if an appellate court allowed damages before 1971 (see Point II) or after 1979 (see Point IV) the appellate court could set damages without the time and expense of a new trial. That motion was not granted. (R. 5525.)

Another trial, and perhaps another appeal, to resolve the above issues could take five to ten years. Such delay violates Article I, Section 11 of the Constitution of Utah which states:

> All courts shall be open, and every person, for an injury done to him in his person, property, or reputation, shall have remedy by due

> course of law, which shall be administered without denial or unnecessary delay; . . .

B. THIS COURT SHOULD SPECIFY A SIMPLE METHOD TO CALCULATE DAMAGES

But there is a shortcut. If the court adopts the reasoning of *Derenco v Benjamin Franklin Federal Savings and Loan Assn* , 281 Or. 533, 557 P.2d 427 (1978), the case could be resolved in the trial court in a matter of months. And, there would likely be no further appeal.[15]

Derenco was a virtually identical case in Oregon. Derenco borrowed money from Benjamin Franklin to purchase a home. Benjamin Franklin required a monthly payment for annual taxes and insurance on the dwelling. As in the case at bar, Benjamin Franklin held the tax and insurance funds up to one year before payment was made on the taxes and insurance. Derenco claimed that Benjamin Franklin was earning a profit by using the tax and insurance funds (for up to one year) before the taxes and insurance bills were actually paid. Derenco filed a class action seeking an accounting and return of the profits.

The *Derenco* court began its analysis by explaining the difficulty of computing actual profits on the funds:

> The trial judge looked at this complicated computation problem and resolved it with rough justice. He awarded income from the accounts to plaintiffs equal to the interest that was paid by

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[15] *Derenco* was an interlocutory appeal. The *Derenco* court gave a specific formula on how the accounting should be computated. After the interlocutory appeal, the trial court was able to compute individual damages. But the damage formula in *Derenco* was so easy and so clean, that damages were processed in the trial court and there was no further appeal of the Final Judgment. (A later petition for certiorari was denied.)

> defendant on ordinary pass book savings accounts. This is eminently sensible. The defendant is a mutual association. The total cost of all operations, including the maintenance of the reserve accounts as well as their investment, has necessarily been deducted from income before payment of pass book interest. The deposits in question were completely commingled with defendant's other invested funds. The cost of servicing the accounts and investing the funds were not capable of being isolated as separate components of defendant's total expenses.
>
> * * *
>
> Ordering an accounting on earnings from the deposits at pass book rates is a method of determining the extent of the profits as closely as possible. We conclude it is the appropriate measure of recovery in this case. *Id.*, 577 P.2d at 494-5. (Emphasis added.)

Listed below is Judge Rigtrup's computation of damages from 1971 to 1979. (See Findings of Fact and Conclusions of Law included herein as Ex. D, R. 3006.) Note that, each year, the "Average Escrow Balance," and the "Average Expense Rate on Escrow Funds" is different from the preceding or following years. Note also that the "Net Earnings" are different for each of the years from 1971 to 1979.

D MADSEN AVERAGE ESCROW BALANCE
AND LOST INCOME AT NET U.S T-BILL YIELDS
March 3, 1971 to June 30, 1979

Year	Average Escrow Balance	Average T-Bill Yield	Average Expense Rate on Escrow Funds	Net Yield	Net Earnings On Escrow Funds	Cumulative Net Earnings Compounded
1971	$226.70	4.33%	1.16%	3.17%	$ 5.97	$ 5.97
1972	$284.94	4.07%	1.10%	2.97%	$ 8.46	$ 15.04
1973	$157.83	7.03%	1.02%	6.01%	$ 9.49	$ 25.72
1974	$219.72	7.84%	1.00%	6.76%	$14.85	$ 42.56
1975	$335.73	5.80%	1.21%	4.59%	$15.41	$ 60.99
1976	$225.06	4.98%	1.78%	3.20%	$ 7.20	$ 72.06
1977	$318.28	5.27%	1.32%	3.95%	$12.57	$ 89.34
1978	$402.81	7.19%	1.25%	5.94%	$23.93	$119.34
1979	$259.84	10.07%	1.18%	8.89%	$11.55	$134.70
			TOTALS:		$109.43	$134.70

However, in Point II of this brief, Madsen argues that damages should also be paid for the years 1964 to 1971. But in order to follow Judge Rigtrup's system, that would require the trial court judge (on remand) to hear evidence on the "Average Expense Rate" for each of the following years: 1964, 1965, 1966, 1967, 1968, 1969 and 1970. Likewise, the trial court would be required to hear evidence on "Average T-Bill yields" for each of the following years: 1964, 1965, 1966, 1967, 1968, 1969 and 1970. Also the trial court would hear similar evidence for the years 1979, 1980, 1981, 1982, 1983, 1984 1985, 1986, 1987, 1988, 1989 . . . In other words, the trial court would be required to hold a "mini trial" on separate earnings each year for the duration of the trust deed contract. Of course, that process could take many months of trial time. But, all of that

can be changed if this Court follows *Derenco*. According to *Derenco*, the trial court could simply award the "ordinary passbook savings" rate for each year of the damage period.

Indeed, the process is so simple and straight forward that a Master may not even be needed. If damages are computed by simply awarding the "ordinary passbook savings" rate, such computations might be done by clerical personnel, without the need of a fancy "Master." Indeed, most of the "*Derenco* type" of computations might be done by ordinary discovery procedures. Even if a Master is needed, it would obviously be much much easier to allow the (new) Master to simply compute the "passbook savings rate" on pledged funds.

C. STANDARD OF REVIEW AND MARSHALING

This issue is one for the appellate court only, and hence is a question of law. *Simper v Scorup*, 78 Utah 71, 1 P.2d 941, 945 (1931). A trial in *Simper* was held three times. The *Simper* Court determined that the "litigation ought to end." So it gave specific instructions regarding damage calculations, ensuring it would end on remand.

Since this issue does not involve a challenge to a factual or discretionary ruling by the trial court, there is no need to marshal evidence.

CONCLUSION

In conclusion, Madsen contends that Prudential has failed for over 25 years to provide the accounting which was mandated in *Madsen I*. Because Prudential has not come forward with its accounting, the trial court turned the accounting over to a Master.

However, Madsen contends that the Master has committed several errors, and that the work (or reports) of the Master must therefore be vacated.

In summary, the core of this case is an accounting. However, at this stage (after three appeals and thirty years) neither Prudential nor the Master have provided a satisfactory accounting. Therefore, Madsen contends that this Court should remand the case with instructions to conduct the accounting using the "*Derenco* formula."

However, if this Court remands the case, this Court should also instruct the trial court that :

A. The work of the Master must be vacated; and if a Master is needed, a new Master should be appointed.

B. There is no statute of limitations.

C. Damages are not cut off in 1979 (because of § 7-17-4 Utah Code Ann.).

D. Profits earned by Prudential on Madsen's trust fund should be compounded each year until such profits and interest are paid to Madsen.

E. This Court should award pre-judgment interest.

F. The trial court erred by removing duplexes, second homes, and commercial properties from the class.

SPECIAL NOTE

The following objection is provisional only. If the court decides that Madsen has correctly marshaled the evidence in this brief, the objection is withdrawn and there is no reason for the Court to rule on this objection. However, the Court should rule on this objection if this Court strikes or disregards some portions of this brief on the grounds tha the marshaling requirement has not been properly satisfied.

PROVISIONAL OBJECTION TO MARSHALING REQUIREMENT

Appellant has attempted throughout this brief to satisfy the requirements of Rule 24(a)(9) of the *Utah Rules of Appellate Procedure* to marshal the opponent's factual evidence. However, appellant respectfully submits such marshaling subject to the objection that the concept of marshaling violates Article 1, Section 11 of the Constitution of Utah which states:

> All courts shall be open, and every person, for an injury done to him in his person, property, or reputation, shall have remedy by due course of law, which shall be administered without denial or unnecessary delay; . . .

Simply stated, it can be a complicated and time consuming process for an attorney to uncover or research facts which might support the opponent (so-called "devil's advocate"). The expense for such extra research falls upon the client. Thus, a client must pay his own attorney to gather facts supporting the client; but the client must also pay his attorney extra money to gather facts that might oppose the client. (Even in contingent fee cases, the attorney may request a higher percentage if the attorney must take time to gather facts supporting the opponent's case, or the attorney in a contingent fee case might have less time to work on his own client's case after marshaling the opponent's evidence.)

It is respectfully submitted that Anglo-Saxon law is an adversarial process. That means that Client A hires an attorney to tell Client A's side of the story. Then, Client B hires an attorney to tell Client B's side of the story. And the Court decides. It has never

been part of Anglo-Saxon law that a client must pay his attorney to tell both sides of the story.

DATED this 29th day of March, 2007.

ROBERT J. DEBRY & ASSOCIATES
Attorneys for Plaintiff and Appellant

Robert J. DeBry

MAILING CERTIFICATE

I hereby certify that I mailed a true and exact copy of the foregoing Brief this 29th day of March, 2007, to the each of the following (thus mailing two copies to counsel for appellee):

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ADDENDUM

Exhibit	Description.
A	*Madsen v. Prudential Federal Savings & Loan*, 558 P.2d 1337 (Utah 1977)
B	*Madsen v. Prudential Federal Savings & Loan*, 635 F.2d 797 (10th Cir. 1980)
C	*Madsen v. Prudential Federal Savings & Loan*, 767 P.2d 538. (Utah 1988)
D	Findings of Fact and Conclusions of Law, R. 2994-3011
E	Motion that Master Perform an Auxiliary Computation of Damages . . . Prior to March 3, 1971 and . . . After June 30, 1979, R. 5035-37 (And supporting Memorandum and subsequent Madsen letter to Master.)
F	Judge Stirba's Order of January 20, 1998. R. 6791-97
G	Master's Final Report, R. 10370-72
H	Master's Letter to Judge Dever dated September 12, 2003. R. 12760-64
I	Final Judgment, R. 13842-44
J	*Interest on Mortgage Loan Accounts Act* (§ 7-17-1 *et seq*. U.C.A.)

able limits, as determined by the sound discretion of the trial court. Under the circumstances shown, and particularly in view of the answers given, we do not see that the cross-examination which was allowed so transgressed propriety as to constitute error prejudicial to the defendant.

[3] In connection with the foregoing, the following should be observed: Prior to the colloquy above quoted from the record, but after the defendant had taken the stand and given his version of what had happened upon direct examination, his counsel moved the court to suppress any questions about his prior felony convictions on the ground that the records did not reflect that he voluntarily and understandingly entered his pleas of guilty in those cases. It was shown and defendant acknowledged that he was represented by counsel in those cases. Our view is in accord with that taken by the trial court: that in the absence of any indication to the contrary, we presume that the judgments of our courts are valid.[9] This, in addition to the fact that the defendant himself made the choice to raise the issue before the jury, who on the basis of that and the whole evidence, did not believe that there was any reasonable doubt of his guilt, leads us to the conclusion that there was no error and that he was accorded his entitlement of a fair trial.[10]

[4, 5] On the issue raised as to the failure to submit to the jury the lesser and included offense of simple assault, the following is pertinent:

Defendant's attorney stated to the court:

> Your Honor, it has been my advice to my client to move the Court to put in an instruction concerning the lesser, included offense of simple assault, and *my client does not wish to do that.* It would be my recommendation to put one in, but *he does not want to.* [Emphasis added.]

It is undoubtedly within the prerogative of the trial court to submit included offenses if he thinks that the interest of justice so require.[11] But when the defendant indicates that he does not want that done, the trial court is under no duty to disregard his request. If the defendant chooses as a matter of trial strategy to have his case submitted on the "all or nothing" gambit, when he loses, he should not be permitted to do an about face and claim that the trial court committed error in going along with his request, but should have submitted the included offense anyway.[12]

Affirmed. No costs awarded.

HENRIOD, C. J., and ELLETT, MAUGHAN and WILKINS, JJ., concur.

Richard MADSEN and Nancy A. Madsen, his wife, Plaintiffs and Appellants,

v.

PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION, Defendant and Respondent.

No. 14530.

Supreme Court of Utah.

Jan. 14, 1977.

Trustors brought action against trustee and beneficiary under deed of trust to trustors' home executed for purpose of securing promissory note, seeking restitution of profits allegedly earned on money paid to defendant pursuant to deed provision that

9. *State v. Valdez,* 19 Utah 2d 426, 432 P.2d 53; *State v. Seymour,* 18 Utah 2d 153, 417 P.2d 655. We so state in awareness of defendant's arguments, citing *Loper v. Beto,* 405 U.S. 473, 92 S.Ct. 1014, 31 L.Ed.2d 374, and *Boykin v. Alabama,* 395 U.S. 238, 89 S.Ct. 1709, 23 L.Ed.2d 274.

10. *State v. Canfield,* 18 Utah 2d 292, 422 P.2d 196.

11. *State v. Mitchell,* 3 Utah 2d 70, 278 P.2d 618; *State v. Valdez,* footnote 8 above, *State v. Close,* 28 Utah 2d 144, 499 P.2d 287.

12. Ibid; and see *State v. Gellatly,* 22 Utah 2d 149, 449 P.2d 993.

required plaintiffs to make monthly payments to defendant which could apply payments to insurance premiums and taxes or to sums due under deed or note. The Third District Court, Salt Lake County, Bryant H. Croft, J., entered summary judgment for defendant, and plaintiffs appealed. The Supreme Court, Maughan, J., held that fact issue whether payments were pledged property existed, thus precluding summary judgment.

Reversed and remanded.

Crockett, J., filed dissenting opinion in which Henriod, C. J., concurred.

Judgment ⇐181(15)

In action brought by trustors against trustee and beneficiary under deed of trust to trustor's home executed for purpose of securing promissory note, seeking restitution of profits allegedly earned on money paid to defendant pursuant to deed provision, which required plaintiffs to make monthly payments to defendant which could apply payments to insurance premiums and taxes or to sums due under deed or note, which contained all essential elements of a pledge, and which granted security interest to defendant, fact issue whether such payments were pledged property existed, thus precluding summary judgment. U.C.A.1953, 70A–9–207(2); U.C.C. § 9–207.

Robert J. DeBry, Salt Lake City, for plaintiffs-appellants.

Joseph J. Palmer, Salt Lake City, for defendant-respondent.

MAUGHAN, Justice:

On appeal is a summary judgment granted to defendant, hereafter Prudential, against plaintiffs, hereafter Madsen or trustors. The action is founded upon terms of a deed of trust; and was brought to determine the status of the parties, and the legal consequences pursuant to such terms. We reverse the summary judgment, and remand for further proceedings. Costs are awarded to Madsen. Statutory references are to U.C.A.1953.

Madsens are trustors, and defendant is both the trustee and beneficiary under a deed of trust executed September 21, 1964, for the purpose of securing a promissory note in the sum of $16,800. The security conveyed was the home in which plaintiffs reside.

To protect the security, the trustors further agreed:

2. To keep the buildings and improvements on the above described premises insured against loss by fire, and such other casualties and in such forms of insurance, and in such amounts, and in such companies as may be required by and as may be satisfactory to the beneficiary, for the benefit of the beneficiary, and to pay the premiums therefor promptly when due, and the policies of insurance shall be held by the beneficiary, it being understood, however, that the beneficiary shall in no event be responsible for the sufficiency or form or substance of any policy of insurance, or for the solvency or sufficiency of any insurance company in respect to the insurance herein provided.

. . . . .

4. To pay before delinquent all taxes and assessments affecting said property (including assessments on appurtenant water stock and costs, interest and penalties thereon); and all encumbrances, charges and liens, with interest and penalties on said property or any part thereof, which appear to be or are prior or superior hereto.

In addition to the monthly payments as provided in said note, the trustor agrees to pay to the beneficiary, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said *budget payments are hereby pledged to the beneficiary as additional security for the full performance of this deed of trust and the note secured hereby.* The budget payments so accumulated may be withdrawn by the beneficiary for the payment of taxes or insurance premiums due on the

premises. The beneficiary may at any time, without notice, apply said budget payments to the payment of any sums due under the terms of the deed of trust and the note secured hereby or either of them. Trustor's failure to pay said budget payments shall constitute a default under this trust. [Emphasis supplied.]

Madsen's appeal is predicated on the theory that the monthly budget payments under provision 4 of the instrument constitute a common law pledge. They alleged defendant had invested this pledged property, and earned a substantial profit. An accounting is sought on the ground the substantial profits from the investment of the pledged funds constitute an unjust enrichment, entitling them to restitution.

The trial court ruled the funds accumulated, from the monthly budget payments, were not pledged property. Therefore, the law of pledge was not applicable.

In *Campbell v. Peter*[1] this court stated:

> A pledge is really one of the simplest forms of security. It is the passing of possession of a chattel by the owner thereof to the pledgee who is thereby entitled to hold it until the debt is paid or the obligation performed. [Citations]

We further cited with approval the definition in the Restatement Security, Sec. 1, p. 5, which provides:

> A pledge is a security interest in a chattel or an intangible represented by an indispensable instrument, the interest being created by a bailment for the purpose of securing the payment of a debt or the performance of some other duty.

Comment d. of Sec. 1, p. 10 states:

> The term "chattel" means any physical object which is capable of manual delivery and which is not the subject-matter of real property. It includes instruments and documents.

A deposit of money as security for the performance of a contract has been recognized as a valid pledge.[2]

> it [is] of no consequence that the amount of funds subjected to the lien, and thus, the amount of the lien, may vary during the existence of the pledge. The amount is ascertainable at any given time, and thus the lien is perfected as to amount.[3]

In the current matter, plaintiffs, as the trustors, agreed to protect the security of Prudential by paying the insurance and taxes. Madsen agreed to pay the budget payments, and to pledge them to the beneficiary "as additional security for the full performance" of the deed of trust and the note secured thereby.

The essential elements of a pledge are contained in the agreement, viz., the existence of a debt or obligation, a transfer of property to the pledgee, to be held as security and, if necessary, to be used to assure performance of the obligation. Furthermore, the payments accumulated, may, in the discretion of the beneficiary, be withdrawn for the payment of taxes, insurance premiums due, or any sum *due* under the deed of trust, or note. There is no contract right granted to Madsen to compel defendant to pay the insurance premiums or taxes. The payments accumulated may be retained as security or applied for the purposes stated. The primary obligation to pay the insurance, taxes, and any sum due under the deed of trust or note is Madsen's. The provisions of section 4 grant a security interest to Prudential, for the purpose of securing performance of trustors' obligations.

Madsen cites *Hoyt v. Upper Marion Ditch Company*[4] to establish the legal consequences, under a common law pledge, wherein profits accrue to pledgee; as a result of the possession of a pledged chattel. We there said it is the duty of a pledgee to collect the accruals, from the security, and

1. 108 Utah 565, 568, 162 P.2d 754, 755 (1945)

2. *Anderson v Pacific Bank*, 112 Cal 598, 44 P. 1063 (1896), *United States v Harris*, USDC WD La 1966, 249 F Supp 221, 224, 68 Am Jur.2d, Secured Transactions, Sec. 58, pp. 886–887.

3. *United States v. Harris*, note 2 supra.

4. 94 Utah 134, 143, 76 P.2d 234 (1938)

H

Madsen v. Prudential Federal Sav. & Loan Ass'nC.A.Utah, 1980.

United States Court of Appeals,Tenth Circuit.

Richard MADSEN and Nancy Madsen, his wife, for themselves and all others similarly situated, Plaintiffs-Appellants,
v.
PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION, for itself and all others similarly situated, Defendant-Appellee,
Utah Bankers Association, Intervenor-Appellee.
Richard MADSEN and Nancy Madsen, for themselves and all others similarly situated, Petitioners,
v.
Honorable Aldon J. ANDERSON, Judge of the United States District Court for the District of Utah, Central Division, Respondent.

Nos. 79-1362, 79-1535.

Argued May 6, 1980.
Decided Dec. 3, 1980.
Rehearing Denied Jan. 23, 1981.

Savings and loan association brought suit for declaratory relief, asserting that it was not required to pay interest or account to borrowers on escrowed funds. The United States District Court for the District of Utah, Central Division, Aldon J. Anderson, J., consolidated suit with class action for an accounting and recovery of profits earned by lender on escrowed amounts which action had been brought by borrowers in state court and removed by lender, and granted summary judgment in favor of lender. Borrowers appealed. The Court of Appeals, Seymour, Circuit Judge, held that: (1) since no federal controversy was disclosed on face of borrowers' state court complaint, as amended, removal was improper, and (2) federal court had no subject-matter jurisdiction over declaratory judgment action.

Reversed with directions.

West Headnotes

[1] Federal Courts 170B ⚿242.1

170B Federal Courts
170BIII Federal Question Jurisdiction
170BIII(D) Pleading
170Bk242 Sufficiency of Allegations
170Bk242.1 k. In General. Most Cited Cases
(Formerly 170Bk242)

Defense predicated upon federal law is not enough by itself to confer federal jurisdiction, even though defense is certain to arise. 28 U.S.C.A. §§ 1331, 1337.

[2] Federal Courts 170B ⚿243

170B Federal Courts
170BIII Federal Question Jurisdiction
170BIII(D) Pleading
170Bk242 Sufficiency of Allegations
170Bk243 k. Particular Cases. Most Cited Cases

Because borrowers predicated their suit to recover interest realized from lender's use of escrow fund upon rights created under state law, fact that federal regulations may have created defense to recovery on such claim was immaterial to finding of federal question jurisdiction. 28 U.S.C.A. §§ 1331, 1337, 1441(b).

[3] Removal of Cases 334 ⚿25(1)

334 Removal of Cases
334II Origin, Nature, and Subject of Controversy
334k25 Allegations in Pleadings
334k25(1) k. In General. Most Cited Cases

Even if federal law has preempted state law in area of federal savings and loan regulation, lender's claim of federal preemption raised to defeat common-law contract claim in state court was in the nature of a defense and could not be basis of federal question jurisdiction on removal. 28 U.S.C.A. §§ 1331, 1337, 1441(b).

635 F.2d 797
(Cite as: 635 F.2d 797)

[4] Removal of Cases 334 ⚿19(1)

334 Removal of Cases
334II Origin, Nature, and Subject of Controversy
334k19 Cases Arising Under Laws of United States
334k19(1) k. In General. Most Cited Cases
Application of federal common law to a plaintiff's cause of action is sufficient to invoke federal jurisdiction and thus support removal. 28 U.S.C.A. § 1441(b).

[5] Federal Courts 170B ⚿374

170B Federal Courts
170BVI State Laws as Rules of Decision
170BVI(A) In General
170Bk374 k. Matters of General Jurisprudence; Federal Common Law. Most Cited Cases
In deciding whether rules of federal common law should be fashioned, normally the guiding principle is that a significant conflict between some federal policy or interest and use of state law in the premises must first be specifically shown.

[6] Federal Courts 170B ⚿412.1

170B Federal Courts
170BVI State Laws as Rules of Decision
170BVI(C) Application to Particular Matters
170Bk412 Contracts; Sales
170Bk412.1 k. In General. Most Cited Cases
(Formerly 170Bk412)
Contractual obligations are created by state law.

[7] Federal Courts 170B ⚿412.1

170B Federal Courts
170BVI State Laws as Rules of Decision
170BVI(C) Application to Particular Matters
170Bk412 Contracts; Sales
170Bk412.1 k. In General. Most Cited Cases
(Formerly 170Bk412)
Interpretation and enforcement of contracts are traditionally within province of state courts, and general presumption is in favor of applying state law.

[8] Removal of Cases 334 ⚿19(1)

334 Removal of Cases
334II Origin, Nature, and Subject of Controversy
334k19 Cases Arising Under Laws of United States
334k19(1) k. In General. Most Cited Cases
Given absence of significant conflict between state contract law and federal policy expressed in regulation providing that "except as provided by contract, a federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph," state law was applicable in determining whether lender contracted to pay interest on borrower's escrow account, and thus claim did not arise under laws of United States, as would support removal jurisdiction. 28 U.S.C.A. §§ 1331, 1337, 1441(b).

[9] Federal Courts 170B ⚿243

170B Federal Courts
170BIII Federal Question Jurisdiction
170BIII(D) Pleading
170Bk242 Sufficiency of Allegations
170Bk243 k. Particular Cases. Most Cited Cases
Federal district court had no jurisdiction over lender's action for declaratory relief, asserting that it was not required to pay interest or account to borrowers for profits realized on escrowed funds, since controversy underlying action was one of state law as to whether lender was obligated by its contract with borrowers to pay interest on escrowed funds, and lender's claim was defensive in nature. 28 U.S.C.A. §§ 1331, 1337, 1441(b).

*798 Robert J. DeBry, Salt Lake City, Utah, for plaintiffs-appellants.
Joseph J. Palmer, Salt Lake City, Utah (Reid E. Lewis, Salt Lake City, Utah, with him on the brief) of Moyle & Draper, Salt Lake City, Utah, for defendant-appellee.
*799 Peter W. Billings, of Fabian & Clendenin, Salt Lake City, Utah, for intervenor-appellee.
Milan C. Miskovsky, Gen. Counsel, Harvey Simon,

Acting Associate Gen. Counsel, Michael L. Seablot, Trial Atty., of Federal Home Loan Bank Board, Washington, D. C., on the brief for amicus curiae Federal Home Loan Bank Board.

Before LOGAN, PECK [FN*] and SEYMOUR, Circuit Judges.

FN* Of the United States Court of Appeals for the Sixth Circuit sitting by designation.

SEYMOUR, Circuit Judge.

The Madsens, plaintiffs-appellants, borrowed money from Prudential Federal Savings & Loan Association (Prudential) to purchase a home in 1964. Pursuant to this loan, the Madsens signed a trust deed [FN1] requiring them to make "budget payments" of one-twelfth of the annual estimated taxes and insurance along with their monthly payments of principal and interest. Under the agreement, these budget payments were pledged as additional security for repayment of the loan. The funds were accumulated in a reserve account and used annually for the payment of taxes and insurance.

FN1. The trust deed provides in pertinent part:
"In addition to the monthly payments as provided in said note, the TRUSTOR agrees to pay to the BENEFICIARY, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said budget payments are hereby pledged to the BENEFICIARY as additional security for the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes or insurance premiums due on the premises. The BENEFICIARY may at any time, without notice, apply said budget payments to the payment of sums due under the terms of this deed of trust and the note secured hereby or either of them. TRUSTOR'S failure to pay said budget payments shall constitute a default under this trust."
App., vol. I, at 5.

On March 3, 1975, the Madsens [FN2] filed a class action [FN3] in Utah state court seeking to recover interest realized from Prudential's use of the escrowed funds, based on claims of breach of contract and unjust enrichment. The state trial court granted Prudential's motion for summary judgment. In January 1977, the Utah Supreme Court reversed the summary judgment and remanded for further proceedings. It held that the trust deed contained the essential elements of a pledge, and that under Utah common law a pledgee must account to the pledgor for profits resulting from the use of the pledged property. In October 1977, the Madsens amended their complaint to ask for an accounting and recovery of the profits earned by Prudential on the escrowed amounts. This amended complaint added a defendant class of lenders with similar escrow arrangements.

FN2. The original complaint named Richard Madsen only as plaintiff. An amended complaint was filed April 10, 1975, joining his wife Nancy.

FN3. Numerous issues regarding the classes named in these proceedings have been raised on appeal. They are not relevant to our disposition of this case and are not addressed in our opinion.

Meanwhile in April 1977, Prudential filed a separate action for declaratory relief in federal court, asserting that under 12 C.F.R. s 545.6-11(c) [FN4] (hereinafter referred *800 to as section 545.6-11(c)), it is not required to pay interest or account to the Madsens on the escrowed funds. The complaint based jurisdiction on 28 U.S.C. s 1337 [FN5] and sought a declaration of the rights and obligations of the parties to the trust deed. When the Madsens amended their state complaint, Prudential promptly filed a removal petition, alleging that the relief requested arises under and is controlled by federal law. The Utah Bankers Association, a trade

association of commercial banks domiciled in Utah, intervened in the action, and the Federal Home Loan Bank Board filed an amicus curiae brief. The federal court denied the Madsens' motion to remand the case, consolidated the removed action and the declaratory judgment suit, and granted summary judgment in favor of Prudential.

FN4. 12 C.F.R. s 545.6-11(c) provides:
"A Federal association which makes a loan on or after June 16, 1975, on the security of a single-family dwelling occupied or to be occupied by the borrower (except such a loan for which a bona fide commitment was made before that date) shall pay interest on any escrow account maintained in connection with such a loan (1) if there is in effect a specific statutory provision or provisions of the State in which such dwelling is located by or under which the State-chartered savings and loan associations, mutual savings banks and similar institutions are generally required to pay interest on such escrow accounts, and (2) at not less than the rate required to be paid by such State-chartered institutions but not to exceed the rate being paid by the Federal association on its regular accounts (as defined by Section 526.1 of this chapter). Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph." (Emphasis added).

FN5. 28 U.S.C. s 1337 provides:
"The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies."

On appeal, the Madsens contend, inter alia, that the federal court lacks jurisdiction over either the removed case or the declaratory judgment action. We agree, and reverse with directions to remand the removed action to state court and to dismiss the declaratory action.

I.

Removal Jurisdiction

Prudential sought removal pursuant to 28 U.S.C. s 1441(b), which provides in pertinent part:
"Any civil action of which the district courts have original jurisdiction founded on a claim or right arising under the Constitution, treaties or laws of the United States shall be removable without regard to the citizenship or residence of the parties."

Jurisdiction was claimed under 28 U.S.C. s 1331 [FN6] and section 1337 because the cause of action allegedly arose under the laws of the United States and Acts of Congress regulating commerce.

FN6. 28 U.S.C. s 1331(a) provides in pertinent part:
"The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and arises under the Constitution, laws or treaties of the United States."
We note that the same standards apply to whether the issue "arises under" federal law in both this section and section 1337.

The Madsens contend their claim in state court is founded upon contract rights and obligations created by state law. They assert that Prudential retains the Madsens' budget payments for up to a year before using the funds to pay the taxes and insurance, that Prudential invests the funds in the interim and receives a profit, and that the Madsens are entitled to be paid the profits earned on the pledged funds. The Madsens point out that no federal law or regulation was invoked, relied on, attacked, or cited in their complaint. Consequently, they say, their claim did not arise under federal law.

Prudential and Intervenor argue, on the other hand, that the trust agreement between Prudential and the

Madsens contains no express language requiring the payment of interest on the escrowed funds, and that the federal regulation does not contemplate interest payments under such circumstances. They say that interpretation of the agreement arises under federal law because Prudential is a regulated federal savings and loan association and Congress has preempted the area.

[1] The conditions under which a suit may be said to "arise under" the laws of the United States were definitively set out in Gully v. First National Bank, 299 U.S. 109, 57 S.Ct. 96, 81 L.Ed. 70 (1936). There the Court stated that the required federal right or immunity must be an essential element of the plaintiff's cause of action, and that the federal controversy must be "disclosed upon the face of the complaint, unaided by the answer or by the petition for removal." Id. at 113, 57 S.Ct. at 98. It is beyond argument that a defense predicated upon ***801** federal law is not enough by itself to confer federal jurisdiction, even though the defense is certain to arise. Pan American Petroleum Corp. v. Superior Court, 366 U.S. 656, 663, 81 S.Ct. 1303, 1307, 6 L.Ed.2d 584 (1961); Seneca Nursing Home v. Kansas State Board of Social Welfare, 490 F.2d 1324, 1328 (10th Cir. 1974), cert. denied, 419 U.S. 841, 95 S.Ct. 72, 42 L.Ed.2d 69 (1974); Warner Bros. Records, Inc. v. R. A. Ridges Distributing Co., 475 F.2d 262 (10th Cir. 1973).

In Mountain Fuel Supply Co. v. Johnson, 586 F.2d 1375, 1381 (10th Cir. 1978), cert. denied, 441 U.S. 952, 99 S.Ct. 2182, 60 L.Ed.2d 1058 (1979), we described the test for determining whether a complaint asserts, on its face, a substantial federal question:
"A case 'arises' under the laws of the United States if it clearly and substantially involves a dispute or controversy respecting the validity, construction or effect of such laws which is determinative of the resulting judgment. Shulthis v. McDougal, 225 U.S. 561, 32 S.Ct. 704, 56 L.Ed. 1205 (1912). Thus, if the action is not expressly authorized by federal law, does not require the construction of a federal statute and/or regulation and is not required by some distinctive policy of a federal statute to be determined by application of federal legal principles, it does not arise under the laws of the United States for federal question jurisdiction. Lindy v. Lynn, 501 F.2d 1367 (3rd Cir. 1974)."

No argument has been made on appeal that the Madsens' claim is expressly authorized by federal law. Consequently, federal removal jurisdiction is established in this case only if the Madsens' claim requires the construction of a federal regulation or the application of federal law.

The federal trial court based its finding of jurisdiction on North Davis Bank v. First National Bank, 457 F.2d 820 (10th Cir. 1972). We find that case distinguishable. There the central issue in the complaint was whether the defendant's facility constituted a branch of a national bank. We noted that the Supreme Court in First National Bank v. Dickinson, 396 U.S. 122, 133, 90 S.Ct. 337, 343, 24 L.Ed.2d 312 (1969), held this determination to be a "threshold question of federal law." 457 F.2d at 822. Therefore we held: "(t)his is not a case in which a federal statute is indirectly or collaterally involved but it is one having its source in and arising under (the McFadden Act) 12 U.S.C. s 36(f). " Id. at 823.

[2] Here the basic issue in the Madsens' complaint is whether the contract between the Madsens and Prudential requires the payment of profits or interest on escrowed funds. Although construction of the federal regulation cited by Prudential may be relevant to the defense Prudential asserts, i. e., that section 545.6-11(c) does not require payment of interest, the meaning of the regulation is absolutely irrelevant to the Madsens' theory of recovery. Because the Madsens have predicated their suit upon rights created under state law, the fact that federal regulations may create a defense to recovery on such a claim is immaterial to a finding of federal question jurisdiction. See Phillips Petroleum Co. v. Texaco, 415 U.S. 125, 94 S.Ct. 1002, 39 L.Ed.2d 209 (1974); Pan American Petroleum, 366 U.S. at 662-64, 81 S.Ct. at 1307-1308.

[3] Prudential and Intervenor contend that removal jurisdiction exists because federal law has preempted state law in the area of federal savings and loan regulation. The amicus curiae brief supports the argument that the field of regulatory

control over federal associations has been preempted. However, even if federal preemption were established, it would not confer jurisdiction when it is raised by the defendant to defeat a common-law contract claim brought in state court. See Pan American Petroleum, 366 U.S. at 662-65, 81 S.Ct. at 1307-1309; Washington v. American League of Professional Baseball Clubs, 460 F.2d 654, 660 (9th Cir. 1972), and cases cited therein. In Home Federal Savings & Loan Association v. Insurance Department, 571 F.2d 423 (8th Cir. 1978) , the court dismissed the case for lack of subject matter jurisdiction despite a federal preemption argument:

***802** "(T)he Commissioner's proceeding against Home Federal was based solely upon alleged violations of Iowa's insurance law and raised no federal question. Home Federal's allegations of preemption and failure to engage in the 'business of insurance,' asserted in its federal petition, actually are in the nature of defenses to the Commissioner's charges. Hence they will not suffice for federal question jurisdiction here. The case is basically simply an alleged violation of state law. It is not a federal case and is not converted to one by Home Federal's defenses to the state's basic allegations."

Id. at 427. Prudential's claim of federal preemption is in the nature of a defense to the Madsens' cause of action and cannot be the basis of federal question jurisdiction on removal.

It is also argued that the Madsens' claim arises under the laws of the United States because the contract must be interpreted under federal common law rather than state law. This is so, Prudential urges, because the regulation addressing the payment of interest by federal savings and loan associations, section 545.6-11(c), states that " (e)xcept as provided by contract, a Federal Association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph." (Emphasis added). Prudential contends that the circumstances constituting a " contract" within the meaning of the federal regulation is a federal question.

[4][5] It is true that the application of federal common law to a plaintiff's cause of action is sufficient to invoke federal jurisdiction and thus support removal. See Illinois v. Milwaukee, 406 U.S. 91, 100, 92 S.Ct. 1385, 1391, 31 L.Ed.2d 712 (1972). However, federal common law is not automatically applied to resolve all disputes in a field subject to pervasive federal regulation. "In deciding whether rules of federal common law should be fashioned, normally the guiding principle is that a significant conflict between some federal policy or interest and the use of state law in the premises must first be specifically shown." Wallis v. Pan American Petroleum Corp., 384 U.S. 63, 68, 86 S.Ct. 1301, 1304, 16 L.Ed.2d 369 (1966). Here, it is vigorously argued that application of state law would create a significant conflict because federal policy requires uniform nationwide standards for the handling of escrow accounts by federal savings and loan associations. This argument founders on the very language of the regulation cited to support it. Section 545.6-11(c) provides that a federal savings and loan association shall pay interest on escrow accounts if a state statute requires such payments to be made by state-chartered institutions, or if payments are required by contract. The regulation expressly anticipates that the obligation of a federal institution to pay interest on escrow accounts not only will vary from state to state, but from contract to contract. See Johnson v. First Federal Savings & Loan Association, 418 F.Supp. 1106, 1109 (E.D.Mich.1976). Any argument that federal policy requires nationwide uniformity with regard to this issue is untenable. [FN7] See United States v. Yazell, 382 U.S. 341, 86 S.Ct. 500, 15 L.Ed.2d 404 (1966).

FN7. We note Intervenor's argument that this case arises under federal law because the mortgage form must be approved by the regulatory agency, see 24 C.F.R. s 203.17, and because the mortgage must provide for monthly escrow payments for taxes and insurance, see 24 C.F.R. s 203.23(a). However, these regulations are silent on the issue of interest payments on escrow accounts, and therefore do not conflict with section 545.6-11(c), which allows interest to be required or prohibited by the individual contract terms.

> Accordingly, we reject the argument that the use of these forms mandates a uniform interpretation under federal law.

[6][7][8] Contractual obligations are created by state law. See Gully, 299 U.S. at 114-15, 57 S.Ct. at 98-99. See also Pan American Petroleum v. Superior Court, 366 U.S. at 662-663, 81 S.Ct. at 1307-1308. "The interpretation and enforcement of contracts is (sic) traditionally within the province of state courts," Mariniello v. Shell Oil Co., 511 F.2d 853, 858 (3d Cir. 1975), and the general presumption is in favor of applying state law. Note: Federal Common Law, 82 Harv.L.Rev. 1512 (1969) . Given ***803** the absence of a significant conflict between the federal policy expressed in section 545.6-11(c) and the use of state law, we hold that state law is applicable in determining whether Prudential contracted to pay interest on the Madsens' escrow account.

Since no federal controversy was disclosed on the face of the Madsens' state court complaint, as amended, removal was improper and the consolidated case must be remanded to state court.

II.

Declaratory Judgment Jurisdiction

[9] The question remains whether the federal court has subject matter jurisdiction over Prudential's declaratory judgment action. The federal complaint alleges that Prudential is a federal savings and loan association regulated by the Federal Home Loan Bank Board, that it makes residential real estate loans insured and guaranteed by federal agencies, and that it is not permitted to pay interest or to otherwise account for profits realized on escrowed funds paid by mortgagors "except as provided by applicable federal regulations." App., vol. II, at 180. It points out that the Madsens have filed a class action in state court seeking interest on the escrowed funds under the contractual arrangements between Prudential and its borrowers, that "(a) proper resolution of said controversy requires a declaration of the respective rights and obligations of the parties to said contractual arrangements," id. at 181, and that this determination presents a question under federal laws regulating commerce or under federal common law.[FN8]

> FN8. We have already concluded in part I, supra, that federal common law is not applicable to interpret the contract between Prudential and the Madsens.

As we have noted, the federal regulation that Prudential cites in its complaint provides that interest shall be paid on escrow accounts if a statute in the state where the mortgaged property is located requires similar lending institutions to pay such interest. 12 C.F.R. 545.6-11(c), supra n. 4. The regulation also provides that a federal association has no other obligation to pay such interest " (e)xcept as provided by contract." Id. Consequently, the controversy underlying the federal declaratory judgment action is the same as in state court: whether Prudential is obligated by its contract with the Madsens to pay interest on the escrowed funds.

This court has consistently adopted the rationale set out by the Supreme Court in Public Service Commission of Utah v. Wycoff Co., 344 U.S. 237, 248, 73 S.Ct. 236, 242-243, 97 L.Ed. 291 (1952):
"Where the complaint in an action for declaratory judgment seeks in essence to assert a defense to an impending or threatened state court action, it is the character of the threatened action, and not of the defense, which will determine whether there is federal-question jurisdiction in the District Court. If the cause of action, which the declaratory defendant threatens to assert, does not itself involve a claim under federal law, it is doubtful if a federal court may entertain an action for a declaratory judgment establishing a defense to that claim. This is dubious even though the declaratory complaint sets forth a claim of federal right, if that right is in reality in the nature of a defense to a threatened cause of action. Federal courts will not seize litigations from state courts merely because one, normally a defendant, goes to federal court to begin his federal-law defense before the state court begins the case under state law. (citations omitted)."

(Emphasis added). In Monks v. Hetherington, 573 F.2d 1164, 1167 (10th Cir. 1978), we applied the traditional view "that a party cannot by artful pleading anticipate a defense based on federal law and thus bring within federal jurisdiction an action that could not otherwise be heard in federal court." And in Chandler v. O'Bryan, 445 F.2d 1045, 1055-56 (10th Cir. 1971), we noted that this principle is particularly applicable where, as here, the state court action ***804** has been instituted and issues have been decided.

We held in part I, supra, that the federal preemption argument is defensive in nature. This is true whether the claim is made as the basis of removal or to support federal jurisdiction in a declaratory judgment action. See, e. g., Home Federal Savings & Loan Association v. Insurance Department, 571 F.2d 423 (8th Cir. 1978). This case is not like Conference of Federal Savings & Loan Associations v. Stein, 604 F.2d 1256 (9th Cir. 1979) , aff'd mem., 445 U.S. 921, 100 S.Ct. 1304, 63 L.Ed.2d 754 (1980), First Federal Savings & Loan Association v. Greenwald, 591 F.2d 417 (1st Cir. 1979), or others cited by Prudential, Intervenor, and amicus curiae, where state regulations directly conflict with federal regulations governing federal associations. No such conflict exists here.

The defensive nature of Prudential's claim is expressed throughout its complaint. It alleges that a state action has been brought seeking interest pursuant to the contractual arrangements between the parties, and that any order of the state court requiring Prudential to pay interest or otherwise account to the Madsens would be contrary to the federal regulations. If the Madsens had attempted to bring their action in federal court by anticipating or responding to Prudential's possible federal defense, the case would lack federal jurisdiction. See Phillips Petroleum, 415 U.S. at 128, 94 S.Ct. at 1004; Skelly Oil Co., 339 U.S. 667, at 672, 70 S.Ct. 876, 879, 94 L.Ed. 1194; Home Federal Savings & Loan Association, 571 F.2d at 426-27. It is irrelevant for purposes of jurisdiction that "federal consent is the source of state authority." Gully, 299 U.S. at 116, 57 S.Ct. at 99; Oklahoma ex rel. Wilson v. Blankenship, 447 F.2d 687, 691 (10th Cir.), cert. denied, 405 U.S. 918, 92 S.Ct. 942, 30 L.Ed.2d 787 (1971).

Here as in Gully "(t)he most one can say is that a question of federal law is lurking in the background. " 299 U.S. at 117, 57 S.Ct. at 99-100. Accordingly, we hold the court has no jurisdiction over the declaratory judgment complaint and the action must be dismissed.

Reversed.

C.A.Utah, 1980.
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(Cite as: 767 P.2d 538)

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Madsen v. Prudential Federal Sav. and Loan Ass'nUtah,1988.

Supreme Court of Utah.

Richard MADSEN and Nancy Madsen, his wife, for themselves and all others similarly situated, Plaintiffs and Appellants,

v.

PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant and Appellee.

No. 860148.

Dec. 30, 1988.

The Third District Court, Salt Lake County, Philip R. Fishler, J., entered an order which disqualified another judge after he had presided over a trial and had orally announced his ruling but before he had entered formal findings of fact, conclusions of law, and final judgment. Opponents of disqualification appealed. The Supreme Court, Stewart, J., held that: (1) the motion to disqualify the judge was not timely; (2) the judge's remarks did not evidence prejudice so as to justify disqualification; and (3) the judge did not have a financial interest in the outcome of the case.

Reversed and remanded.

Zimmerman, J., concurred in the result.

West Headnotes

[1] Judges 227 ⚿51(2)

227 Judges
227IV Disqualification to Act
227k51 Objections to Judge, and Proceedings Thereon
227k51(2) k. Time of Making Objection. Most Cited Cases

Party who has reasonable basis for moving to disqualify judge may not delay in hope of first obtaining favorable ruling and then complain only if result is unfavorable. Rules Civ.Proc., Rule 63(b).

[2] Judges 227 ⚿51(2)

227 Judges
227IV Disqualification to Act
227k51 Objections to Judge, and Proceedings Thereon
227k51(2) k. Time of Making Objection. Most Cited Cases

To be timely, motion to disqualify judge should be filed at counsel's first opportunity after learning of disqualifying facts; only if good cause for delay is demonstrated in motion seeking disqualification should delinquent motion even be considered. Rules Civ.Proc., Rule 63(b).

[3] Judges 227 ⚿51(2)

227 Judges
227IV Disqualification to Act
227k51 Objections to Judge, and Proceedings Thereon
227k51(2) k. Time of Making Objection. Most Cited Cases

Party's motion to disqualify judge was not filed "as soon as practical after * * * bias or prejudice" was known; party failed to raise issue during colloquy with judge before his ruling, party failed to object after ruling was made when objections were invited by judge, and party delayed 39 days after trial to file its disqualification motion. Rules Civ.Proc., Rule 63(b).

[4] Judges 227 ⚿40

227 Judges
227IV Disqualification to Act
227k40 k. Constitutional and Statutory Provisions. Most Cited Cases

While most of the Code of Judicial Conduct is aimed exclusively at the regulation of judicial behavior, Canon relating to disqualification not only regulates judicial conduct, but also seeks to avoid unfairness by insuring each litigant an impartial judge. Code of Jud.Conduct, Canon 3, subd. C.

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[5] Judges 227 ⚿49(2)

227 Judges
227IV Disqualification to Act
227k49 Bias and Prejudice
227k49(2) k. Statements and Expressions of Opinion by Judge. Most Cited Cases
Judge was not required to disqualify himself from action in which bank was defendant, despite judge's statement that many years earlier he had "cussed financial institutions." U.C.A.1953, 78-7-1; Code of Jud.Conduct, Canon 3, subd. C.

[6] Judges 227 ⚿49(2)

227 Judges
227IV Disqualification to Act
227k49 Bias and Prejudice
227k49(2) k. Statements and Expressions of Opinion by Judge. Most Cited Cases
As long as a judge does not allow personal propensities to obscure the evidence and will decide the case only after all the evidence is heard, disqualification is generally not warranted by a judge's comments. Code of Jud.Conduct, Canon 3, subd. C.

[7] Judges 227 ⚿42

227 Judges
227IV Disqualification to Act
227k41 Pecuniary Interest
227k42 k. In General. Most Cited Cases
For purposes of claim a judge should have disqualified himself from case involving bank, judge did not have "financial interest" in case, despite the fact that judge was former borrower from that bank because the judge had no ownership interest as required by the Code of Judicial Conduct.

[8] Judges 227 ⚿49(1)

227 Judges
227IV Disqualification to Act
227k49 Bias and Prejudice
227k49(1) k. In General. Most Cited Cases
Judge who heard case involving bank, and who was former borrower of that bank, did not have "any other interest" in litigation, so as to require disqualification. U.C.A.1953, 78-7-1; Code of Jud.Conduct, Canon 3, subd. C.

*539 Robert J. DeBry, Salt Lake City, for plaintiffs and appellants.
Joseph J. Palmer, Reid E. Lewis, Salt Lake City, for defendant and appellee.
STEWART, Justice:
Plaintiffs Richard and Nancy Madsen appeal a district court order entered by Judge Philip Fishler which disqualified Judge Kenneth Rigtrup after he had presided over a trial in this case and had orally announced his ruling but before he had entered formal findings of fact, conclusions of law, and final judgment. Judge Fishler ruled that Judge Rigtrup had no actual bias, but did have an appearance of bias and voided the trial and all prior orders entered by Judge Rigtrup in the case.

This appeal is yet another installment in the protracted history of this case, which started in 1975 and has already been before this Court once, *Madsen v. Prudential Fed. Sav. & Loan Ass'n,* 558 P.2d 1337 (Utah 1977), and before a federal appellate court once, *Madsen v. Prudential Fed. Sav. & Loan Ass'n,* 635 F.2d 797 (10th Cir.1980), *cert. denied,* 451 U.S. 1018, 101 S.Ct. 3007, 69 L.Ed.2d 389 (1981). The facts which gave rise to this litigation are reported in detail in those opinions. 558 P.2d at 1338-39; 635 F.2d at 799-800.

Plaintiffs are representatives of a certified class of borrowers whose trust deeds with Prudential Federal Savings and Loan Association (hereafter " Prudential") contained language identical to that contained in the Madsens' trust deed. In 1984, this action was assigned to Third District Court Judge Kenneth Rigtrup who had been assigned to four other similar cases.[FN1] Prudential appeared as amicus curiae in each of the other actions.

FN1. *Roger Hal Read and Elizabeth W. Read,* for themselves and all others similarly situated *v. American Equity Corporation,* for itself and all others similarly situated, district court No.

C-244219 (filed August 11, 1977). *James W. Petty and Mary E Petty,* for themselves and all others similarly situated *v. Western Savings and Loan Co.,* district court No. C-79-700 (dismissed July 19, 1983). *Russell R Everill and Helen B. Everill,* for themselves and all others similarly situated *v Western Savings and Loan Co.,* district court No. C-79-701 (dismissed July 19, 1983). *Ernest H. Dixon and Lori Ann P. Dixon,* for themselves and all others similarly situated *v United Savings and Loan Ass'n,* district court No. C-79-1105 (filed February 16, 1979).

The issue here was whether a financial institution which loaned money to the plaintiffs on a first trust deed is obligated to pay interest to the plaintiffs on monthly budget payments for property taxes and insurance that are paid with the monthly mortgage payments. In a bench trial in September 1985, the Madsens and Prudential tried the limited issue of whether Prudential made any profit on the budget payments it collected from the Madsens. At the close of the trial, Judge Rigtrup ruled from the bench. Just prior to his ruling, the following exchange occurred between Judge Rigtrup and counsel for the parties:

THE COURT: ... I'll share the benefits of my decision with you at this point.

... I'll expose my biases and my prejudices and be very frank with you.

I think there are some substantial kinds of policy things that have really caused me great trouble and trauma. As I've indicated earlier, and no objection was interposed, I was a customer of Prudential Federal Savings & Loan Association and paid without default for 25 years at four and three-quarters per cent, ... and I computed that out and I thought, why, those robbers, they are charging me twice what I'm borrowing from them, and that's unfair.

As I get older and more sophisticated I-

MR. PALMER [Attorney for Prudential]: Your Honor, I hate to interrupt, but I need to make the point that this is news to me, that you had been a customer of Prudential.

THE COURT: I indicated that on several occasions.

MR. PALMER: I beg the Court's pardon, but that is news to me. I don't ***540** recall that at all-if anybody else does-recall you telling me that, and I-

THE COURT: I indicated that in these earlier meetings that I had paid my loan off at some point, and I'd had a loan with Prudential Federal Savings.

MR. PALMER: Perhaps the Court is thinking of conferences with other counsel. The reason I make the point is-

THE COURT: My earlier conferences were not with the two of you in this case, they were with Mr. Billings, with Mr. Ashton, with you, with Mr. Giauque, Mr. McDonough, with respect to whoever he represents. It was Mr. Giauque or someone from that office. They were a corrective kind of a deal.

MR. PALMER: In any event, I stand to raise the point now that it is news to us. I believe it-I take it that the Court did not feel that it had any prejudice because of that.

THE COURT: No.

MR. PALMER: All right.

THE COURT: I have a recollection that somewhere along the line I did make that disclosure. I don't know how you could be part of the community and be a homeowner and not have borrowed from someone. And so I think I make it very clear in one of those collective kinds of meetings that my loan had been with Prudential Federal.

At any rate, it's a fact, and it was something that I never tried to hide or have hid from anyone. So there's no sense of covering up. I guess if that creates error, it creates error. But so be it. I have a recollection that I did expose it, and whether you were there or Mr. Lewis or anyone else, I don't know. I did make the disclosure early on.

MR. DeBRY [Attorney for the Madsens]: I do recall some conversations, I think, off the record, of that effect, and I honestly don't recall who was present. But it was a comment that was made from time to time.

MR. PALMER: Could I inquire of the Court when the loan was paid off?

THE COURT: Probably two years ago. I'm not sure at what point in the discussions I indicated that, but I'm sure that in the presence of the collective group that I indicated that I had been a borrower of Prudential Federal Savings.

MR. PALMER: No prejudice arose in the Court's

mind because of the fact that we collected a mortgage escrow from you?
THE COURT: No.
MR. PALMER: Okay. I can't do anything else but ask.
THE COURT: That's what I've been trying to tell you. That was the intention.
MR. PALMER: I make the point because I didn't want to go on and let the Court note-
THE COURT: I think I've made general comments throughout that I have cussed financial institutions, and customers do simply because they see inherent injustice about that. And my perspective today, after 23 years has passed, has become much, much different at the end of the 23 years. Far before that I could see the cost of money was markedly greater, and that I would be a damn fool to prepay. So I paid faithfully every month for 25 years, and not a day sooner or a day later. And I'm just commenting generally in terms of unjust or whatever. The tension is between that to be gained and that to be lost, I suppose, in my eyes. And I have a feeling that class actions are a form of champerty and maintenance in that the one that substantially gains is the lawyer or the expert. Mr. Madsen stands to gain little, except he has struck a blow for freedom, I suppose, in the form that the consumer has achieved balance.
Be seated, Mr. DeBry.
MR. DeBRY: I want to make an objection on the record. I really must.
THE COURT: Well, sit down.
MR. DeBRY: Before you give your decision, I must make a comment, because I know the Court is being candid and this has been a long struggle, and Prudential says they are almost broke before this.
And you say maybe DeBry will make some money, but I haven't yet. But I really must interpose an objection at this ***541** point. If the Court harbors this type of personal bias with respect to-
THE COURT: I'm just-
MR. DeBRY: -class actions.
THE COURT: I'm just telling you about the tension.
MR. DeBRY: I must object to the Court's sitting on this case if you have that kind of bias.
THE COURT: I'm just telling you why I'm getting to my ruling and how I'm getting to my ruling and being open and candid with both of you. But that's a built-in problem with class actions. They have achieved a beneficial result. The difficult[y] I am locked into is that I have got to follow the law of the case. I have got the Supreme Court that's telling me what to do....
....
MR. DeBRY: Your Honor-
THE COURT: You can take exceptions after I get done. I'm trying to-
MR. DeBRY: I might note that I do have an exception to take at this time before you give your verdict in this matter.
THE COURT: I haven't given a verdict.

Prudential did not object during the course of the exchange. Judge Rigtrup rendered his decision in favor of the Madsens and awarded them damages of $134.70.

After the ruling, Judge Rigtrup asked if either side wished to take any exceptions. Prudential's attorney stated only that an appeal was anticipated before any class issues were addressed. However, no specific objection to Judge Rigtrup's qualifications was voiced.

Thirty-nine days after Judge Rigtrup announced his decision, Prudential raised its first formal objection to the judge's qualifications to hear the case by filing a motion for disqualification under Rule 63(b) of the Utah Rules of Civil Procedure.[FN2] The motion was assigned to the then-presiding judge of the Third District, the Honorable Philip Fishler. Judge Fishler held several hearings on the motion and considered testimony, portions of the trial transcript, affidavits, and memoranda in reaching his decision. Judge Fishler ruled that Prudential's motion was timely, that the possibility existed that Judge Rigtrup may have a financial interest in the outcome of the case, and that Judge Rigtrup's impartiality might reasonably be questioned. Judge Fishler expressly found no actual bias on the part of Judge Rigtrup, but ordered him disqualified solely on the appearance of bias. After the case was assigned to another judge for retrial, we granted plaintiffs' request for an interlocutory appeal of Judge Fishler's order.

FN2. Rule 63(b) reads:
(b) *Disqualification.* Whenever a party to any action or proceeding, civil or criminal, or his attorney shall make and file an affidavit that the judge before whom such action or proceeding is to be tried or heard has a bias or prejudice, either against such party or his attorney or in favor of any opposite party to the suit, such judge shall proceed no further therein, except to call in another judge to hear and determine the matter.
Every such affidavit shall state the facts and the reasons for the belief that such bias or prejudice exists, and shall be filed as soon as practicable after the case has been assigned or such bias or prejudice is known. If the judge against whom the affidavit is directed questions the sufficiency of the affidavit, he shall enter an order directing that a copy thereof be forthwith certified to another judge (naming him) of the same court or of a court of like jurisdiction, which judge shall then pass upon the legal sufficiency of the affidavit. If the judge against whom the affidavit is directed does not question the legal sufficiency of the affidavit, or if the judge to whom the affidavit is certified finds that it is legally sufficient, another judge must be called in to try the case or determine the matter in question. No party shall be entitled in any case to file more than one affidavit; and no such affidavit shall be filed unless accompanied by a certificate of counsel of record that such affidavit and application are made in good faith.

I.

The Madsens contend that Prudential waived its objections to Judge Rigtrup's qualifications by failing to make a timely objection at the time of the judge's exchange with counsel, thereby giving Prudential the advantage of waiting to see if the ruling was favorable and, if not, of moving to disqualify. In addition, Prudential*542 waited an extended period to file its motion to disqualify.

[1] While a motion to disqualify a judge should not be undertaken lightly, it must be made promptly. A party who has a reasonable basis for moving to disqualify a judge may not delay in the hope of first obtaining a favorable ruling and then complain only if the result is unfavorable. Not only is such a tactic unfair, but it may evidence a belief that the judge is not in fact biased. Furthermore, delay imposes unnecessary disruption on both the judicial system and litigants. A disqualification proceeding is a collateral attack on the substantive action, it disrupts orderly litigation, and it necessarily results in significant additional costs to the parties. Accordingly, a party must move with dispatch once a basis for disqualification is discovered. *See Duplan Corp v. Deering Milliken, Inc.,* 400 F.Supp. 497, 508-10 (D.S.C.1975); *Hunnicutt v Hunnicutt,* 248 Ga. 516, 518, 283 S.E.2d 891, 893 (1981). *See generally* L. Abramson, *Judicial Disqualification Under Canon 3C of the Code of Judicial Conduct* 11-12 (1986) [hereinafter L. Abramson, *Judicial Disqualification*].

Timeliness is essential in filing a motion to disqualify.[FN3] In Utah, disqualification motions in civil proceedings are governed by Rule 63(b) of the Utah Rules of Civil Procedure (set out in footnote 2). That rule requires that a disqualification motion "shall be filed as soon as practicable after the case has been assigned or such bias or prejudice is known." The issue in this case is whether Prudential's failure to raise the issue during the colloquy with the judge before the ruling, its failure to object after the oral ruling was made when objections were invited by Judge Rigtrup, and Prudential's delay of thirty-nine days after the trial to file its disqualification motion meet the "as soon as practicable" requirement of Rule 63(b).

FN3. Some jurisdictions impose specific time limitations on some disqualification motions. *See, e.g.,* 28 U.S.C. § 144 (1982) (affidavit of bias must be filed not less than ten days before the beginning of the term at which the proceeding is to be heard); Alaska Stat. § 22.20.022(c) (1984) (affidavit for peremptory removal of judge must be filed within 5 days after the case is

at issue or within 5 days after the issue is assigned to a judge); Me.Rev.Stat.Ann. title 14, § 1103 (1980 & Supp.1988) (petition for change of judge must be filed within ten days after service of complaint or other application for which equitable relief is sought); Minn.R.Civ.P. 63.03 (notice to remove judge must be filed within ten days after a party receives notice of which judge is presiding at the trial or hearing, but no later than commencement of the trial or hearing).

Federal cases require that motions to disqualify must be made as soon as the facts which form the basis for the disqualification become known. *See United States v. Studley,* 783 F.2d 934, 939 (9th Cir.1986) ("a motion for recusal filed weeks after the conclusion of a trial is presumptively untimely absent a showing of good cause for its tardiness"); *Singer v. Wadman,* 745 F.2d 606, 608 (10th Cir.1984), *cert. denied,* 470 U.S. 1028, 105 S.Ct. 1396, 84 L.Ed.2d 785 (1985) (motion to disqualify filed one year after complaint and after adverse rulings of trial court was untimely); *Wood v. McEwen,* 644 F.2d 797, 802 (9th Cir.1981), *cert. denied,* 455 U.S. 942, 102 S.Ct. 1437 (1982) (delay of sixteen months after grounds for disqualification arose made motion to disqualify untimely); *United States v. Patrick,* 542 F.2d 381, 390 (7th Cir.1976), *cert. denied,* 430 U.S. 931, 97 S.Ct. 1551, 51 L.Ed.2d 775 (1977) ("The law is well settled that one must raise the disqualification of the judge at the earliest moment after knowledge of the facts demonstrating the basis for such disqualification."); *Satterfield v. Edenton-Chowan Bd. of Educ.,* 530 F.2d 567, 574 (4th Cir.1975) ("One must raise the disqualification of the trier, whether he be a judge, an administrator, or an arbitrator, at the earliest moment after knowledge of the facts."); *Davis v. Cities Serv. Oil Co.,* 420 F.2d 1278, 1282 (10th Cir.1970) (motion to disqualify filed a month after the case was decided against movants is too late); *Duplan Corp. v. Deering Milliken, Inc.,* 400 F.Supp. 497, 510 (D.S.C.1975) ("a recusal motion must be made at counsel's *first opportunity after discovery* of the disqualifying facts" (emphasis in original)).

***543** State courts have also imposed stringent timeliness requirements. *See, e g., Wakefield v. Stevens,* 249 Ga. 254, 255, 290 S.E.2d 58, 60 (1982) (motion to disqualify untimely if not "filed promptly and without delay, at the first opportunity after ... [learning] of the grounds for disqualification " (quoting*State v. Fleming,* 245 Ga. 700, 705, 267 S.E.2d 207, 210 (1980) (Hill, J., concurring))); *Carpenter v. State,* 223 Kan. 523, 525, 575 P.2d 26, 29 (1978) (affidavit of prejudice should be filed as soon as a party "becomes aware of the facts giving rise to the challenge"). The rule is stated in 46 Am.Jur.2d *Judges* § 202, at 225-26 (1969):

It is a well-recognized rule that an application for the disqualification of a trial judge must be filed at the earliest opportunity. The courts generally apply this rule with strictness against a party who, having knowledge of facts constituting a disqualification, does not seek to disqualify the judge until an unfavorable ruling has been made.

(Footnotes omitted).

[2] While the Utah rule imposes no specific time limitation on the filing of a motion for disqualification, timeliness is still essential. To be timely, a motion to disqualify should be filed at counsel's first opportunity after learning of the disqualifying facts. Only if good cause for a delay is demonstrated in the motion seeking disqualification should a delinquent motion even be considered. *See Davis,* 420 F.2d at 1282; *Duplan Corp.,* 400 F.Supp. at 509-10.

[3] Prudential's motion to disqualify Judge Rigtrup was not timely. Prudential claims that its first notice of bias on Judge Rigtrup's part occurred in his statement prior to announcing his ruling. However, Prudential's attorney did not object to the judge's continued participation in the case, as did opposing counsel, nor did Prudential ask for a continuance to consider disqualification. Prudential's attorney merely responded "that this is news to me" and then, after further dialogue with the judge, allowed the proceedings to continue without objection. By contrast, the *Madsens' counsel* did object to Judge Rigtrup's continuation as trial judge.

Prudential claims that Judge Rigtrup seemed determined to quell all interruptions as evidenced by his repeated admonition to plaintiffs' counsel to " sit down." Nevertheless, the record set out above demonstrates that plaintiffs' counsel was able to object. Beyond that, moments after Judge Rigtrup had delivered his oral ruling, he specifically afforded Prudential another opportunity to object: " Do you desire to make any further exceptions...." Prudential's attorney responded: "Well, what I'm suggesting is that I expect that there will be an appeal before we get into the class issues, and I would anticipate findings and a judgment be presently entered in favor of Mr. Madsen." However, no mention was made of "recusal" or " disqualification."

Prudential asserts that it did object at trial, but our review of the record discloses no objection. On the contrary, it discloses Prudential's apparent acquiescence in Judge Rigtrup's rendering a decision.

Finally, Prudential waited thirty-nine days after the ruling to file a formal motion to disqualify. Prudential argues that it had good cause for the delay. It contends that the lengthy delay was necessary to review personal notes, discuss the matter with other counsel in related cases, discuss the matter with Prudential's officers, and order, receive, and review a partial transcript. However, the review of the attorney's notes and the discussions with others should have consumed no more than a day or two. We doubt that the transcript was essential; in any event, all the facts relating to disqualification were known to Prudential's attorney at the close of the proceedings and an affidavit of prejudice and motion to disqualify could have been prepared with only a knowledge of those facts. We see no reason why the affidavit of prejudice and motion to disqualify should have taken more than ten days to prepare and file, especially since this case was at an advanced stage. Prudential failed to act with sufficient promptness in a ***544** matter which, by its very nature, requires promptness.

In sum, Prudential's motion to disqualify was not filed "as soon as practicable after ... bias or prejudice is known," as required by Rule 63(b). Indeed, for all that appears, Prudential was not convinced at the time of the ruling that Judge Rigtrup should have recused himself.

II.

Given the importance of impartiality and the duty of a judge to recuse him- or herself *sua sponte* when necessary, we next address the issue of whether Judge Rigtrup should have disqualified himself on his own motion. In this context, we analyze the issues of apparent and actual bias raised by Prudential and addressed by Judge Fishler in his ruling.

Standards for judicial disqualification are established by statute and the Code of Judicial Conduct, which this Court adopted in 1974 and which is patterned after the ABA Code of Judicial Conduct of 1972. Utah Code Ann. § 78-7-1 (1987) provides for disqualification if the judge is a party, has an interest in a case, is related to either party, or has been an attorney for either party in the action. [FN4] The statute allows a waiver of disqualification if both parties consent, a point not at issue here.

FN4. Utah Code Ann. § 78-7-1 reads in full:
Disqualification for interest or relation to parties.
Except by consent of all parties, no justice, judge or justice of the peace shall sit or act as such in any action or proceeding:
(1) to which he is a party, or in which he is interested.
(2) when he is related to either party by consanguinity or affinity within the third degree, computed according to the rules of the common law.
(3) when he has been attorney or counsel for either party in the action or proceeding.
But the provisions of this section shall not apply to the arrangement of the calendar or the regulation of the order of business, nor to the power of transferring the action or proceeding to some other court.

Canon 3 C of the Code of Judicial Conduct (hereafter "Code") is more comprehensive than the statute in prescribing instances when judicial disqualification is warranted. In this case, the parties have based their arguments for and against disqualification on the Code. For this reason, we address the disqualification issues in the context of the Code.

[4] The Madsens contend that the Code is an ethical code only and that a violation of the Code should not result in the invalidation of all of a judge's previous rulings. They argue that a violation should result only in discipline of the judge and not in a penalty to an innocent party who may have expended large amounts of time and money only to have a large part of the lawsuit invalidated because of a judicial disqualification. While most of the Code is aimed exclusively at the regulation of judicial behavior, Canon 3 C not only regulates judicial conduct, but it also seeks to avoid unfairness by insuring each litigant an impartial judge. Because we conclude that disqualification of the trial judge was not appropriate, we do not address further the issue of retroactive invalidation of a trial judge's rulings.

Prudential argues that Judge Fishler was correct in disqualifying Judge Rigtrup because Judge Rigtrup had personal knowledge of disputed evidentiary facts, displayed bias against Prudential, and had a financial interest in the outcome of the case. These allegations impute actual bias, but Judge Fishler specifically found no actual bias.[FN5] Moreover, as shown below, ***545** none of Prudential's allegations of bias withstands scrutiny.

> FN5. Obviously, actual bias need not be found to support disqualification. *See State v. Neeley,* 748 P.2d 1091, 1094 (Utah 1988). An appearance of bias or prejudice is sufficient for disqualification, but even disqualification because of appearance must have some basis in fact and be grounded on more than mere conjecture and speculation. In close cases, disqualification is the favored course of action. However, disqualification is not automatic and the basis for disqualification should be thoroughly examined, especially in cases such as this which are at an advanced stage of the litigation process. *See, e.g., In re Virginia Elec. & Power Co.,* 539 F.2d 357, 364 (4th Cir.1976). As is demonstrated elsewhere in this opinion, close examination of Prudential's allegations against Judge Rigtrup show them to be without merit. Therefore, there was no basis in this case for disqualification.
>
> We note that disqualification due to the appearance of bias or prejudice seems more amenable to prospective application. The purpose of disqualification based on appearance of bias is "to promote public confidence in the judicial system by avoiding even the appearance of partiality." *Health Services Acquisition Corp. v. Liljeberg,* 796 F.2d 796, 800 (5th Cir.1986), *aff'd,* 486 U.S. 847, 108 S.Ct. 2194, 100 L.Ed.2d 855 (1988). In *Liljeberg v. Health Services Acquisition Corp.,* 486 U.S. 847, 108 S.Ct. 2194, 2202-03, 100 L.Ed.2d 855 (1988), the United States Supreme Court concluded that disqualifying facts which a federal district judge should have known but which he had forgotten were sufficient to disqualify the judge under the federal statute. However, the federal statute in question, 28 U.S.C. § 455(a) (1982), requires disqualification for an appearance of bias.
>
> Canon 3 C(1) makes disqualification based on an appearance of bias discretionary ("A judge *should* disqualify himself ...") (emphasis added).

A.

First, Prudential argues that Judge Rigtrup had personal knowledge of disputed evidentiary facts and, thus, violated Canon 3 C(1)(a). The issue before Judge Rigtrup was whether Prudential earned a net profit on the Madsens' budget payments. Prudential claimed a net loss in the handling of such funds. Prudential asserts that it had waived insurance premium payments of certain

borrowers, including Judge Rigtrup, in 1977 and gave those borrowers the option of continuing their escrow accounts or discontinuing them altogether in 1979. For that reason, Prudential asserts, the judge had independent knowledge of the disputed issue from which Judge Rigtrup "jumped to the conclusion in his ruling that Prudential could have and would have discontinued the Madsens' reserve, or otherwise changed its handling procedures, rather than lose money in requiring them."

Judge Fishler was not persuaded that Judge Rigtrup had any knowledge concerning the facts in dispute in this case and found that this allegation would not support a claim of bias. Judge Fishler was correct. Although Judge Rigtrup had knowledge of his own dealings with Prudential some six and eight years before the trial, that knowledge did not bear on the issue of whether Prudential made a profit on the budget payment accounts. Prudential cites no record support to the contrary.

B.

[5] Next, Prudential argues that remarks made by Judge Rigtrup just before delivering his ruling evidenced prejudice. Prudential specifically asserts here, as it did before Judge Fishler, that the remarks made by the judge, including the comment, "I have cussed financial institutions, ..." revealed a bias that warranted disqualification. Judge Fishler's memorandum decision does not mention this allegation as a basis for his disqualification order.

Concededly, Judge Rigtrup was somewhat less than diplomatic in expressing what his thinking had been many years ago about financial institutions and how his thinking had evolved over the years. Nevertheless, Judge Rigtrup's own remarks in context explain the isolated instances thought by Prudential to show bias. The judge stated:

I think I've made general comments throughout that I have cussed financial institutions, and customers do simply because they see inherent injustice about that. And my perspective today, after 23 years [have] passed, has become much, much different at the end of the 23 years. Far before that I could see the cost of money was markedly greater, and that I would be a damn fool to prepay. So I paid faithfully every month for 25 years, and not a day sooner or a day later. And I'm just commenting generally in terms of unjust or whatever. The tension is between that to be gained and that to be lost, I suppose, in my eyes. And I have a feeling that class actions are a form of champerty and maintenance in that the one that substantially gains is the lawyer or the expert. Mr. Madsen stands to gain little, except he has struck a blow for freedom, I suppose, in the form that the consumer has achieved balance.

Later the judge stated:The tension is that in terms of the magnitude of the wear, what is to be ***546** gained by Mr. Madsen is de minimis. On the other hand, if the Court looks at economic realities, the high cost of money, high cost of labor and high cost of everything else, there is a societal interest in maintaining healthy, vital financial institutions that have the ability to fund building construction, homes, and so forth, in our community. And I simply observe that probably the savings and loan associations have been very instrumental and important in that particular process. I simply make those as an overview statement say to [sic] what has troubled me, and it's trouble[d] me for a long time.

[6] Canon 3 C(1)(a) states that a judge should disqualify himself if he has "personal bias or prejudice concerning a party." Although litigants are entitled to a judge who will hear both sides and decide an issue on the merits of the law and the evidence presented, they are not entitled to a judge whose mind is a clean slate. Each judge brings to the bench the experiences of life, both personal and professional. A lifetime of experiences that have generated a number of general attitudes cannot be left in chambers when a judge takes the bench. Refusing to disqualify himself in *Laird v. Tatum,* 409 U.S. 824, 93 S.Ct. 7, 34 L.Ed.2d 50 (1972), Justice Rehnquist responded to a motion to recuse *nunc pro tunc:*

Proof that a Justice's mind at the time he joined the Court was a complete *tabula rasa* in the area of constitutional adjudication would be evidence of lack of qualification, not lack of bias.

....

[N]either the oath, the disqualification statute, nor the practice of the former Justices of this Court guarantees a litigant that each judge will start off from dead center in his willingness or ability to reconcile the opposing arguments of counsel with his understanding of the Constitution and the law.

Id at 835, 838-39, 93 S.Ct. at 14, 15-16 (memorandum opinion of Rehnquist, J.) (emphasis in original). One commentator has stated.Supreme Court Justices are strong minded men, and on the general subject matters which come before them, they do have propensities; the course of decision cannot be accounted for in any other way.

J. Frank, *Disqualification of Judges· In Support of the Bayh Bill,* 35 Law & Contemp. Probs. 43, 48 (1970). Obviously, the same is true for all judges. Concerning comments made in court during a case, a commentator stated:The traditional judicial view is that if a judge can be disqualified for bias following a comment or ruling during the court proceedings, there is no limit to disqualification motions and there would be a return to "judge shopping." Any judicial comment or ruling gives the appearance of partiality in the broadest sense to the adversely affected party. Suppose a judge who is the trier of fact comments during a hearing that a parent has had the opportunity to improve himself in order to make a home for his child but has made no effort to do so. Can the judge be disqualified for bias and prejudice? Whenever a judge hears any evidence, he develops an attitude which may change as the evidence develops. As long as the judge decides the case only after *all* the evidence is submitted, there appears to be no harm in such a comment. Such judicial comments made before a jury would constitute an improper expression of opinion on the evidence, but those statements made out of their hearing do not require recusal.

L. Abramson, *Judicial Disqualification,* at 23 (emphasis in original) (footnotes omitted). As long as a judge does not allow the "propensities" to obscure the evidence and will decide the case only after all the evidence is heard, then disqualification is generally not warranted by a judge's comments. *See Banks v. Department of Human Resources,* 141 Ga.App. 347, 348-49, 233 S.E.2d 449, 450 (1977), *overruled on other grounds, Chancey v. Department of Human Resources,* 156 Ga.App. 338, 340, 274 S.E.2d 728, 730 (1980).

*547 Judge Rigtrup's remark that he had "cussed financial institutions" was simply a statement about an attitude he had had many years earlier, at a time when he was less knowledgeable about the operations of financial institutions. Viewed in its entirety and in the context in which that statement was made, there is no evidence of disqualifying bias in Judge Rigtrup's remarks. Indeed, it appears that Prudential saw no impropriety at the time the remarks were made, as demonstrated by its failure to object.

C.

[7] Prudential next contends that because Judge Rigtrup was at one time a Prudential borrower, he had a financial interest in the outcome of the case. Prudential claims that the judge is either a "potential " member of the existing plaintiff class or a " potential" member of an alleged plaintiff class which has never been certified. This "potential" membership, Prudential claims, gives Judge Rigtrup sufficient financial interest in the outcome of the case to warrant disqualification. Prudential asserts that amended complaints filed by the Madsens have added new legal theories to the case and have sought enlargement of the plaintiff class. The result, Prudential claims, is a plaintiff class whose boundaries are imprecise.

Notwithstanding Prudential's assertions, this case has a precisely defined plaintiff class, consisting of Prudential borrowers whose trust deeds contain language identical to the Madsens' trust deed. The class was certified by Judge Croft in 1977. Prudential does not argue, and we find nothing in the record to indicate, that Judge Rigtrup is a member of that class. While it is true that the Madsens did seek to enlarge the class, a new plaintiff class has never been certified. Allegations alone do not act to enlarge an existing class.

Judge Fishler held that Judge Rigtrup "*may* therefore *have a financial interest* which would be

substantially affected by the outcome of the proceeding as defined under Canon 3C(1)(c)." (Emphasis added.) Judge Fishler erred. Judge Fishler and both sides on appeal have overlooked a critical point-the meaning of the term "financial interest" in Canon 3 C(3)(c).

Canon 3 C(3)(c) states that " *'financial interest' means ownership* of a legal or equitable interest, however small, or a relationship as director, advisor, or other active participant in the affairs of a party...." (Emphasis added). In other words, without an ownership interest, no financial interest exists.

In *Virginia Elec & Power Co. v Sun Shipbldg. & Dry Dock Co.,* 407 F.Supp. 324 (E.D.Va.), *vacated sub nom on other grounds In re Virginia Elec. & Power Co.,* 539 F.2d 357 (4th Cir.1976), a trial judge was asked to disqualify himself because he was a customer of the plaintiff public utility, and a verdict favorable to the plaintiff could result in a personal benefit to the judge of approximately $100 realized as a reduction in utility rates. The judge stated:
Clearly, whatever interest the Court may have in the subject matter in controversy, it does not constitute a "financial interest" as defined [by the Code of Judicial Conduct and 28 U.S.C. § 455]. It has " ownership" of no interest-legal or equitable.... [T]he Court actually has "a vague and undefined interest, not ownership, in a credit or accounting adjustment...."

407 F.Supp. at 327. The United States Court of Appeals for the Fourth Circuit reversed on other grounds but stated in its opinion that the trial judge correctly concluded that "he did not 'own' a legal or equitable interest in the subject matter." *In re Virginia Elec & Power Co.,* 539 F.2d 357, 366 (4th Cir 1976). The appellate court noted that the trial judge's interest was analogous to a "bare expectancy " in property law and concluded that "Judge Warriner 'owned' just what the owner of a bare expectancy has-nothing at all." *Id.* at 367.

Judge Rigtrup also owned nothing. Therefore, he had no financial interest in the case as defined by Canon 3 C(3)(c), and disqualification on this basis was unwarranted.

***548** D.

[8] Finally, while Prudential has not raised the issue, we briefly examine whether Judge Rigtrup's disqualification would be warranted under the portion of Canon 3 C(1)(c) which calls for disqualification when the judge or a close relative has "any other interest that could be substantially affected by the outcome of the proceeding...." The Reporter for the Code of Judicial Conduct interpreted "any other interest" to mean an economic interest. E. Thode, *Reporter's Notes to Code of Judicial Conduct* 63-67 (1973). Unlike the term "financial interest," "any other interest" does not require ownership and includes lesser economic interests. At least one trial judge has disqualified himself after finding that "any other interest" includes the possibility of receiving a $100 rebate on utility payments. *Virginia Elec. & Power Co.,* 407 F.Supp. 324. It could therefore be argued that Judge Rigtrup's potential membership in an alleged class constitutes "any other interest" and requires disqualification.

Although the term "any other interest" is usually confined to economic interests, further definition of the exact types of economic interests which fall under the ambit of the term is difficult.[FN6]

FN6. For a discussion of the few cases which classify noneconomic interests as " any other interest," see L. Abramson, *Judicial Disqualification,* at 65; C. Wright, A. Miller & E. Cooper, 13A *Federal Practice and Procedure* § 3547, at 605 (1984). *See also Health Services Acquisition Corp. v. Liljeberg,* 796 F.2d 796, 800 n. 1 (5th Cir.1986), *aff'd,* 486 U.S. 847, 108 S.Ct. 2194, 100 L.Ed.2d 855 (1988); *Liljeberg v. Health Services Acquisition Corp.,* 486 U.S. 847, 108 S.Ct. 2194, 2206, 100 L.Ed.2d 855 (1988).

In any event, the interest must be "substantially affected" to require disqualification. Professor

Wright has stated: "The concept [of 'any other interest'] is necessarily an imprecise one. It has been suggested that it should be read 'to depend on the interaction of two variables: the remoteness of the interest and its extent or degree.' " C. Wright, A. Miller, & E. Cooper, 13A *Federal Practice and Procedure* § 3547, at 603 (1984) (footnotes omitted). Another frequently cited article has illustrated the point as follows:

If the interest strongly resembles a direct interest-for example, stock held in a subsidiary (or parent) of the corporate party-any amount should disqualify, just as does any stock held in the party itself. As the interest becomes less direct, such as that in an enterprise carrying on business with the party, only if the extent of the interest is itself substantial can the judge's impartiality reasonably be questioned.

Note, *Disqualification of Judges and Justices in the Federal Courts,* 86 Harv.L.Rev. 736, 753 (1973) (footnote omitted).

Courts which have considered the issue have followed this approach, examining both the nature of the interest and the extent of the interest. In *In re Virginia Elec. and Power Co.,* the Fourth Circuit relied on that approach to hold that a trial judge's interest in a possible rebate on utility payments was a de minimis interest and that disqualification was not required. 539 F.2d at 368. *See also Alaska Oil Co. v. Alaska,* 45 Bankr. 358, 361-62 (D.Alaska 1985).

Aetna Life Ins. Co. v. Lavoie, 475 U.S. 813, 106 S.Ct. 1580, 89 L.Ed.2d 823 (1986), is similar in significant respects to this case. In *Aetna,* the insurer discovered after an opinion had been issued that a justice of the Alabama Supreme Court who was the author of the per curiam opinion had filed two actions against insurers in state court alleging issues nearly identical to those presented to the court on appeal. One of the suits involved only that justice. The other was a class action in which the class apparently included all members of the Alabama Supreme Court. The United States Supreme Court addressed separately the disqualification issue with respect to the individual justice and the other members of the Alabama court as members of the uncertified class. The Court held that the individual justice should have recused himself because the opinion which he had authored had "the clear and immediate effect of enhancing both the legal status and the settlement value of his own case." ***549**475 U.S. at 824, 106 S.Ct. at 1586 . However, the Court refused to hold that the other members of the Alabama court should have been disqualified because of their potential status as members of a class of plaintiffs in a class action lawsuit. The United States Supreme Court stated:

Any interest that they might have had when they passed on the rehearing motion was clearly highly speculative and contingent. At the time, the trial court had not even certified a class, let alone awarded any class relief of a pecuniary nature.... At some point, "[t]he biasing influence ... [will be] too remote and insubstantial...."

475 U.S. at 826, 106 S.Ct. at 1558 (quoting *Marshall v. Jerrico, Inc.,* 446 U.S. 238, 243, 100 S.Ct. 1610, 1613, 64 L.Ed.2d 182 (1980)).

In this case, Judge Rigtrup is, at most, a potential member of an alleged class. As such, his position is similar to eight of the nine justices of the Alabama Supreme Court in *Aetna* who might have found themselves class members. Under those circumstances, the United States Supreme Court refused to find in favor of disqualification, and we do likewise here. If any existing certified classes are expanded to include Judge Rigtrup or any new class were certified that included him, Judge Rigtrup would have to disqualify himself from further proceedings. We assume, of course, that he would not undertake to rule on a motion to certify a class or to expand a class if he could thereby become a party by virtue of his ruling.

REVERSED AND REMANDED.

HOWE, Associate C.J., and DURHAM, J., concur.
ZIMMERMAN, J., concurs in the result.
HALL, C.J., does not participate herein.
Utah,1988.
Madsen v. Prudential Federal Sav. and Loan Ass'n
767 P.2d 538

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IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT
IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiffs, vs. PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION, for itself and all others similarly situated, Defendants.	FINDINGS OF FACT AND CONCLUSIONS OF LAW Civil No. 226073 JUDGE KENNETH RIGTRUP

PREAMBLE

On September 4, 5, and 6, 1985, this case was tried to the Court without a jury. Plaintiff was represented by Robert J. DeBry. Defendant was represented by Joseph Palmer and Reid E. Lewis.

Although this is a class action, the Court has ordered the parties to present evidence during this stage of the proceedings only for Madsen individually.

At the outset of the trial, Madsen made a motion to bifurcate, and demanded a jury to hear evidence on a Statute of

Limitations issue: viz. when Madsen knew or should have known of Prudential's alleged misconduct (Motion to Bifurcate, August 27, 1985). Prudential made a Motion to Strike the Jury Demand (August 30, 1985). The Court ruled that the discovery rule would not toll the statute of limitations and that the request for a jury trial was therefore denied. In making its ruling, the court announced that:

(a) When the Madsens entered the contract, they got a copy of it and they had an opportunity to read it before they signed it.

(b) The contract made no provision about interest specifically.

(c) The Madsens knew or should have known about the absence of interest provisions in the contract.

(d) The Madsens could have ascertained Prudential's financial circumstances if profits or interest had been of any concern to them.

(e) The Madsens were members or shareholders of Prudential and, as such, they were entitled to examine business records and books and obtain a profit and loss statement and to inquire into such documents.

Prudential contended that there were 24 additional

issues in the case. Prudential timely reserved the following issues in this case:

(a) Whether the parties intended earnings to be paid or whether, considering all circumstances, including their conduct, the benefit the Madsens received, and the industry custom and practice, they intended a special agreement that earnings not be paid.

(b) Whether the parties intended a true pledge relationship or a debtor-creditor relationship.

(c) Whether the budget funds are pledged property or a commingled, fungible cash deposit.

(d) Whether Prudential was unjustly enriched by use of the budget funds.

(e) Whether payment of earnings on the Madsens' budget funds has been preempted by federal law and regulations of the Federal Home Loan Bank Board as a matter of fact and of law, since 1964.

(f) Whether the Madsens have waived their claims, or they are barred by estoppel or laches from asserting them.

(g) Whether the Madsens' budget account is a "short term savings account" within the meaning of 12 C.F.R. § 541.5.

Prudential made the following offer of proof to support their affirmative defenses:

(a) Affidavit of Edwin Calvert.

(b) Affidavit of Gibbs Marsh.

(c) Prudential's Answers to Interrogatories.

(d) Prudential's Charter (1977).

(e) Deposition of Arthur Liebold.

(f) Deposition of plaintiff Madsen.

(g) Documents produced by the Federal Home Loan Bank Board.

(h) Prudential's annual reports.

(i) Briefs on appeal.

(j) Unspecified testimony of Mr. Adams -- an auditor of Prudential Federal.

The offer of proof was received and denied. Rather, the Court limited the scope of this trial to whether Prudential has earned a profit from the use of the pledged funds, and if so, for an accounting of those profits. (Compare, Order, dated September 3, 1985.)

With the case in this procedural posture, and after hearing evidence of the parties, the Court enters the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. Madsen entered into a trust deed contract with Prudential on September 24, 1964.

2. Pursuant to this contract, Madsen was required to make monthly advance payments for anticipated taxes and insurance premiums. These advance payments were known as "budget payments."

3. Payments were prompted by a monthly request for payment, or a bill from Prudential to Madsen.

4. Madsen tendered a single check for his monthly payment. This single check included principle, interest and "budget payment". Madsen submitted this monthly payment together with a copy of the monthly bill or the billing stub. Prudential maintained separate accounting records to credit Madsen for payment of principle, interest and "budget" funds.

5. Upon receiving each monthly payment, Prudential immediately deposited the entire check into its general operating account.

6. Payments for Madsen's taxes and insurance premiums were taken out of this general account as needed periodically. The property taxes and insurance premiums were paid by Prudential on an annual basis. Prudential made annual reports to Madsen about the specific allocation and payment of Madsen budget funds for taxes and insurance premiums.

7. Prudential also used this general operating account for routine business expenses such as office lease

payments, salaries, office machines, etc.

8. Prudential invests most surplus funds from the general operating account in short term investments such as U.S. Treasury Bills, U.S. Treasury Notes, Certificates of Deposit, and certain Federal Agency obligations. However, Prudential also uses the same general operating account to make some longer term investments at higher yields. Prudential earns a profit on all of those investments.

9. It is possible, by using Prudential's financial records, to determine the amount of income which Prudential has received by investing surplus funds from the general operating account. The Court has also determined that a portion of that income is attributable to Madsen's "budget" payments. The income attributable to Madsen's "budget" payments is set forth in Exhibit A attached.

10. In computing that income (paragraphs 8 and 9 above), the Court has assumed that the excess funds were invested in short term Treasury Bills because such Treasury Bills would be liquid and readily available to pay for Madsen's taxes and insurance when due. In fact, in addition to Treasury Bill investments, Prudential made other investments at higher yields.

11. Prudential undergoes a number of procedural steps in order to process tax and insurance bills, and to pay those

amounts on behalf of Madsen. However, the Court specifically finds that Prudential would be performing many of those same steps with or without the "budget" payments. For example, Prudential sends a monthly statement to Madsen. However, Prudential would send that same statement to request the monthly mortgage payment even if there were no "budget" payments.

12. Based upon the evidence in the record, the Court has found the costs which Prudential incurred in handling and managing the "budget" funds, including the cost of processing tax and insurance payments, as included in Exhibit A.

13. The difference between income and expenses on Exhibit A represents profits or earnings which Prudential has realized by its use and investment of Madsen's "budget" funds.

14. The Court finds it appropriate under the facts of this case to compound on an annual basis. The Court finds that Prudential must disgorge these compounded profits in order to make Madsen whole. The compounded earnings are included in Exhibit A.

15. For the period of March 3, 1971 to June 30, 1979, Prudential's earnings or profits realized by using Madsen's "budget" payments amount to $109.43. That amount is increased to $134.70 by compounding on an annual basis up to June 30, 1979.

16. The combined table of the Court's findings on

profits or earnings is attached as Exhibit A.

17. It was not disputed that on or about July 25, 1979, Madsens received a letter from Prudential reproduced at Exhibit B of these findings (or, Exhibit A-1 of Madsen's Third Amended Complaint). Exhibit B is the letter that Prudential mailed out based upon Utah Code Ann. § 7-17-4.

18. It was not disputed that Madsens responded to Prudential's letter of July 25, 1979 in a letter dated September 4, 1979, reproduced at Exhibit C of these findings (or, Exhibit B of the Third Amended Complaint).

19. It was not disputed that Madsen did not withdraw his "budget account" from Prudential after receiving Prudential's letter of July 25, 1979.

CONCLUSIONS OF LAW

1. The law of this case was set by the Utah Supreme Court in the case of Madsen v. Prudential Federal Savings & Loan Assn., 558 P.2d 1337 (Utah 1977), and by the Memorandum Decision of the Honorable Bryant Croft dated June 14, 1977.

2. Specifically, the law of the case is that the "budget" payments made by Madsen for taxes and insurance constitute a common law pledge. If Prudential has realized any profits or earnings from the use of the pledged funds, Prudential

must disgorge those profits to Madsen.

3. This case is an action for an accounting in equity.

4. The applicable statute of limitations for this case is four years, pursuant to § 78-12-25(2), "An action for relief not otherwise provided for by Law." The complaint was filed on March 3, 1975. Therefore, the damage period shall begin on March 3, 1971.

5. Damages terminate on June 30, 1979 by reason of Utah Code Ann. § 7-17-4.

6. Utah Code Ann. § 7-17-4, is not an unconstitutional impairment of contract under U.S. Constitution Article I, Section 10 or Utah Constitution Article I, Section 18. The notice sent by Prudential to Madsen (pursuant to Utah Code Ann. § 7-17-4) does not offend the due process requirements of the U.S. Constitution or the Utah State Constitution since Madsen was represented by counsel who would advise him as to the legal effect of Utah Code Ann. § 7-17-4. Furthermore, neither § 7-17-4 nor the said notice take vested rights from Madsen in violation of Utah Constitution Article I, Section 7, or the Fourteenth Amendment to the United States Constitution.

7. The doctrine which would toll the statute of limitations until the injured party discovers or reasonably

should have discovered the harmful conduct is not applicable to this case (see Preamble).

8. The statute of limitations is not tolled by reason of Madsen's claim that a continuing illegal business practice should toll the statute.

9. The "budget" account is not a "bank deposit" within the meaning of Utah Code Ann. § 78-12-34 .

10. Prudential should be ordered to pay to Madsen the sum of $134.70 for profits or earnings Prudential has realized by using Madsen's "budget" payments for the period of March 3, 1971 to June 30, 1979.

11. Madsen is entitled to his costs of action.

12. All class issues are reserved for further proceedings.

13. Plaintiffs shall have simple interest at the annual rate of 10% on the damages awarded to them in the Court's ruling of September 6, 1985, calculated from that date to the entry of judgment. Plaintiffs shall not be allowed interest for any time prior to trial, for the reasons that the damages were not calculable before trial, that damage calculation at trial was subject to divergent evidence and viewpoints, especially between the parties' expert witnesses, that damages required a determination by the Court and that the Court was required to

select one method of calculation from among several alternatives presented by the experts.

DATED this 22nd day of March, 1990.

BY THE COURT:

By: _____
HONORABLE KENNETH RIGTRUP

Approved as to Form:

_____
ROBERT J. DEBRY

Approved as to Form:

_____
JOSEPH J. PALMER
REID LEWIS

CERTIFICATE OF MAILING

I certify that on the 21 day of March, 1990, I mailed a true and correct copy of the foregoing PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW, (Madsen v. Prudential), U.S. Mail, postage prepaid, to the following:

Joseph J. Palmer
Reid E. Lewis
MOYLE & DRAPER, P.C.
600 Deseret Plaza
Salt Lake City, Utah 84111-1901

Kathy Palmer

SP19-020\jn

INTERNAL EXHIBIT A

R. D. MADSEN
AVERAGE ESCROW BALANCE
AND LOST INCOME AT NET U.S. T-BILL YIELDS

March 3, 1971 To June 30 1979

Year	Average Escrow Balance	Average T-Bill Yield	Average Expense Rate on Escrow Funds	Net Yield	Net Earnings On Escrow Funds	Cumulative Net Earnings Compounded
1971	$226.70	4.33%	1.16%	3.17%	$5.97	$5.97
1972	$284.94	4.07%	1.10%	2.97%	$8.46	$15.04
1973	$157.83	7.03%	1.02%	6.01%	$9.49	$25.72
1974	$219.72	7.84%	1.00%	6.76%	$14.85	$42.56
1975	$335.73	5.80%	1.21%	4.59%	$15.41	$60.99
1976	$225.06	4.98%	1.78%	3.20%	$7.20	$72.06
1977	$318.28	5.27%	1.32%	3.95%	$12.57	$89.34
1978	$402.81	7.19%	1.25%	5.94%	$23.93	$119.34
1979	$259.84	10.07%	1.18%	8.89%	$11.55	$134.70
			TOTALS;		$109.43	$134.70

INTERNAL EXHIBIT B

July 25, 1979

NOTICE TO HOMEOWNERS

RESERVE ACCOUNTS FOR PAYMENT OF TAXES AND INSURANCE

As of July 1, 1979, Prudential Federal Savings will no longer require a reserve account in conjunction with your mortgage loan for the payment of real estate property taxes, insurance premiums, or other charges. You may now choose one of the following two options:

A. You may continue your monthly payment as is now provided for in your loan documents to be deposited in a non-interest bearing reserve account. We will continue to provide you the service of paying your property taxes and/or insurance premiums at no cost as they become due; or,

B. You may elect to assume the legal responsibility for the payment of these assessments and pay your own real estate property taxes, insurance premiums and other charges as they become due.

If you choose Option A, no response is necessary. We will continue to provide the services of paying these assessments without cost to you. If you choose Option B, the enclosed card must be signed and returned to our office by September 1, 1979. Please send this card to:

Prudential Federal Savings and Loan Association
P.O. Box 15500
Salt Lake City, Utah 84115

Attention: Mortgage Loan Servicing

Upon receipt of the card indicating that you wish to pay your own taxes, insurance and other charges on a direct basis, we will return to you the present balance in your reserve account and adjust your monthly payment accordingly.

While Prudential is governed by Federal and not State Law in matters dealing with the terms of a loan contract, the options as set forth herein are consistent with the provisions of Utah Law.

Enclosure

(1) Option Card

INTERNAL EXHIBIT C

September 5, 1979

CERTIFIED MAIL

Prudential Federal Savings & Loan Association
115 South Main Street
Salt Lake City, Utah 84111

Re: Richard and Nancy Madsen
Loan No. 335-018511-6

Gentlemen:

Mr. and Mrs. Madsen have consulted this office in connection with your letter of July 25, 1979 entitled, Notice to Homeowners - Reserve Accounts for Payments of Taxes and Insurance.

It appears that your letter is in violation of the express provisions of the Interest on Mortgage Loan Reserve Accounts Act, § 7-17-1, et seq., Utah Code Ann. (1953). Specifically, your letter has claimed protection under § 7-17-4 Utah Code Ann. (1953); however, § 7-17-4 is clearly not applicable to the Madsen contract. That section provides in part:

> (1) A lender not requiring the establishment and maintenance of a reserve account shall offer the borrower the following options:

We have examined the Madsen contract. As you know, the contract contains a provision requiring the Madsens to make monthly payments into the Reserve Account. We are told by the Madsens that they had no choice in the matter. The contract was presented to them on a "take it or leave it" basis. In short, Prudential has already "required" the Madsens to pay into the reserve account, and that requirement has been reduced to a written agreement. That requirement will, of course, continue to exist for the life of the contract. Thus it seems fair to conclude that the existing contract constitutes a continuing requirement.

We are not aware of any doctrine by which Prudential can now "unrequire" a reserve account. Stated in other words, Prudential cannot unilaterally change the written contract. Nor can the legislature change the written contract.

This analysis is confirmed by the use of the word and in the first sentence of § 7-17-4. Note that the word and is in the conjunctive. In other words, Prudential is entitled to the protection of § 7-17-4 only where both conditions exist conjunctively:

> First, the lender does not require the establishment of a reserve account,
>
> and
>
> second, the lender does not require the maintenance of a reserve account.

Prudential can never satisfy both of these conditions on existing loans. Even if Prudential does not require the maintenance of a reserve account in future, Prudential has nonetheless already required such a reserve for the past several years. The reserve account has already been established. Thus Prudential can never satisfy the first condition of § 7-17-4.

On the other hand, § 7-17-3, Utah Code Ann. (1953), is drafted in the disjunctive:

> (1) Each lender requiring the establishment or continuance of a reserve account in connection with an existing or future real estate loan shall pay interest on funds deposited in the account after June 30, 1979 of at least 4% simple interest per annum ....

Thus, Prudential would fall under § 7-17-3 if it had required the establishment of a reserve account or if Prudential required the continuance of a reserve account. Prudential has already required the establishment of the reserve account by contract. Thus, § 7-17-3 is satisfied. Since the statute is drafted in the disjunctive, it really makes no difference at all that Prudential may somehow discontinue that requirement in the future. Section 7-17-3 is satisfied simply because Prudential required the reserve account in the existing contract.

It is not necessary that both conditions be satisfied.

This all boils down to a fairly simple scenario. Prudential has sent out a series of letters announcing that the policy of requiring a reserve account has been reversed. Prudential next claims that it is entitled to the protection of § 7-17-4 because it has no policy requiring a reserve account. The fallacy in all of this is that the requirement for a reserve account arises from a contract--not a policy. The contract continues to exist. It cannot be changed at the mere whim and caprice of Prudential. The contract constitutes a continuing requirement. Since Prudential's contract requires the reserve account, the transaction falls under § 7-17-3.

In view of the foregoing, we are convinced that the Madsen contract does not fall under § 7-17-4. Thus, pursuant to § 7-17-8(2), Utah Code Ann. (1953), we herewith demand payment of interest pursuant to § 7-17-3, Utah Code Ann. (1953). If you fail to honor this demand, it is our intent to file suit pursuant to § 7-17-8(1), Utah Code Ann. (1953).

It is further apparent that Prudential has sent similar or identical notices to other borrowers. Therefore, pursuant to § 7-17-8(2), Utah Code Ann. (1953), we make this demand on behalf of the Madsens and all other borrowers of Prudential similarly situated.

Moreover, we are informed that every lending institution in Utah has sent letters in substance and effect identical to the Madsen letter. It is inconceivable that all of these lending institutions could misread the simple language of the statute. Rather, we conclude that this parallel conduct is the result of a conspiracy by Utah lending institutions to circumvent the requirements of § 7-17-3. By reason of such industry-wide practice and conspiratorial conduct, all Utah lending institutions are juridically related and subject to treatment as a defendant class under Rule 23 of the Utah Rules of Civil Procedure. Thus, by copy of this letter, we make demand under § 7-17-8(2) on behalf of all borrowers in the

State of Utah who have received letters from any Utah lender in substance and effect similar to the Madsen letter.

Sincerely yours,

Robert J. Mabry

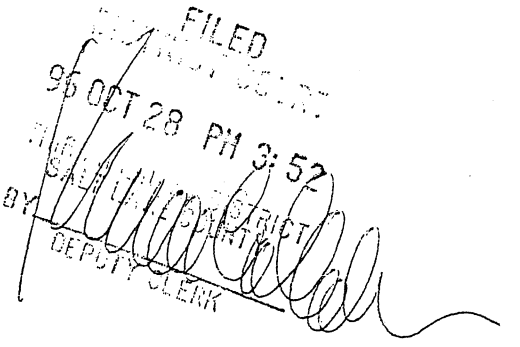
RJD/chh

cc: All Utah State Banks;
All National Banks with their principal place of business in the State of Utah;
All State Savings/Buildings and Loan Associations with their principal place of business in the State of Utah;
All Federal Savings/Building and Loan Associations with their principal place of business in the State of Utah.

bc: Mr. Richard Madsen

WALLACE R. BENNETT - A0286
1723 South 2100 East
Salt Lake City, UT 84108
Telephone: (801) 581-1516

ROBERT J. DEBRY - A0849
ROBERT J. DEBRY & ASSOCIATES
4252 South 700 East
Salt Lake City, UT 84107
Telephone: (801) 262-8915
Attorneys for Plaintiffs



IN THE THIRD JUDICIAL DISTRICT COURT

IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiffs/Appellants, vs. PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant/Appellee.	**MOTION THAT MASTER PERFORM AN AUXILIARY COMPUTATION OF DAMAGES (AT PLAINTIFFS' EXPENSE) FOR PERIODS PRIOR TO MARCH 3, 1971 AND FOR PERIODS AFTER JUNE 30, 1979** Trial No. 750226073 Civil no. C79-8404 HONORABLE KENNETH RIGTRUP

This Court has previously entered Orders that the Master compute damages for class members for the period March 3, 1971 to June 30, 1979.

Plaintiffs move for an Order that the Master perform an auxiliary computation of damages (at plaintiffs' expense) for the periods prior to March 3, 1971 and after June 30, 1979. In support of this Motion, plaintiffs' rely on the memorandum filed herewith.

DATED this 28 day of Oct., 1996.

ROBERT J. DEBRY & ASSOCIATES
Attorneys for Plaintiffs

ROBERT J. DEBRY

Wallace R. Bennett
WALLACE R. BENNETT
(By RJD)

CERTIFICATE OF HAND DELIVERY

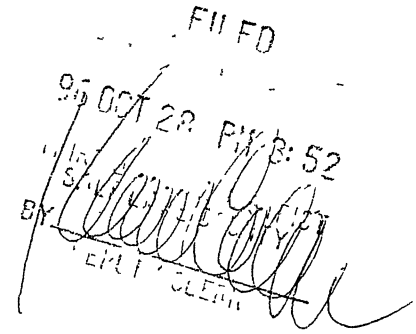
I certify that a true and correct copy of the foregoing PLAINTIFFS' MOTION THAT MASTER PERFORM AN AUXILIARY COMPUTATION OF DAMAGES (AT PLAINTIFF'S EXPENSE) FOR PERIODS PRIOR TO MARCH 3, 1971 AND FOR PERIODS AFTER JUNE 30, 1979 (Madsen v. Prudential), was HAND DELIVERED this 28 day of Oct., 1996, to the following:

Joseph J. Palmer — via hand delivery
PRINCE, YEATES & GELDZAHLER
175 East 400 South, #900
SLC, UT 84111

Edwin Erickson (Master) — via hand delivery
HANSEN, STEED, BRADSHAW & MALMROSE
261 East Broadway, Suite 100
SLC, UT 84111

Linda Lock
Via-runner

sp19.114/lk



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Attorneys for Plaintiffs

IN THE THIRD JUDICIAL DISTRICT COURT

IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiffs/Appellants, vs. PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant/Appellee.	**MEMORANDUM IN SUPPORT OF PLAINTIFFS' MOTION THAT MASTEI PERFORM AN AUXILIARY COMPUTATIOI OF DAMAGES (AT PLAINTIFFS' EXPENSE) FOR PERIODS PRIOR TO MARCH 3, 1971 AND FOR PERIODS AFTER JUNE 30, 1979** Trial No. 750226073 Civil no. C79-8404 HONORABLE KENNETH RIGTRUP

This Court has previously ordered the Master to prepar a damage computation for all class members for the period March 3 1971 to June 30, 1979. The court selected the June 30, 1979 cut off by reason of § 78-12-25(2), Utah Code Ann. (See Conclusion o Law No. 4, March 22, 1990.) The court selected the June 30, 197 cut-off by reason of § 7-17-4, Utah Code Ann. (See Conclusion o Law No. 5, March 22, 1990.)

These cut-off dates were vigorously contested b plaintiffs, and they are not free from doubt. However, those cut

off dates now stand, and the Master is poised to begin a monumental task of computing damages for up to 10,000 class members for the above-described window of time.

This case is now over 20 years old. If the court erred in computing the cut-off dates, the supreme court would be required to send the Master back to recompute the damages for periods outside that window. Of course, the Master would then be required to reassemble all of the records and start all over again. More years would be added.

It is respectfully submitted that the risk of delaying this case for even more years can be avoided by simply permitting the Master, at plaintiffs' expense,[1] to perform damage computations for time periods which plaintiffs believe to be relevant. Then, if an appellate court comes to a different conclusion, on the applicable window of time, it would be a simple matter to adjust the amount of the judgment.

Finally, plaintiffs have offered to pay the cost of the Master for this supplemental calculation;[2] however, plaintiffs specifically offer to pay only the incremental increase, and not a pro-rata share. For example, the current damage window is approximately 8 years. Plaintiffs might seek an auxiliary computation for an additional (say) 16 years. However, plaintiffs are not

---

[1]If the Appellate Court reverses this Court on the applicable window of time, plaintiffs reserve the right to claim reimbursement for these costs in any subsequent proceeding.

[2]But see fn. 1.

offering to pay 2/3s (or 16/24ths) of the Master's cost. Rather defendant should pay the entire cost of the core -- 8 year - study. Plaintiffs would then pay the incremental cost of th actual time needed for the Master to keep extending his computa tions for the extra years.

DATED this 28 day of October, 1996.

ROBERT J. DEBRY & ASSOCIATES
Attorneys for Plaintiffs

ROBERT J. DEBRY

WALLACE R. BENNETT

CERTIFICATE OF HAND DELIVERY

I certify that a true and correct copy of the foregoing PLAINTIFFS' MEMORANDUM IN SUPPORT OF MOTION THAT MASTER PERFORM AN AUXILIARY COMPUTATION OF DAMAGES (AT PLAINTIFF'S EXPENSE) FOR PERIODS PRIOR TO MARCH 3, 1971 AND FOR PERIODS AFTER JUNE 30, 1979 (Madsen v. Prudential), was HAND DELIVERED this 28 day of Oct., 1996, to the following:

Joseph J. Palmer — via hand delivery
PRINCE, YEATES & GELDZAHLER
175 East 400 South, #900
SLC, UT 84111

Edwin Erickson (Master) — via hand delivery
HANSEN, STEED, BRADSHAW & MALMROSE
261 East Broadway, Suite 100
SLC, UT 84111

Linda Lora
Via - Runner

sp19 115/lk

LAW OFFICE
ROBERT J. DEBRY
AND ASSOCIATES

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Orem, Utah 84097
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ST. GEORGE
243 East St. George Blvd. S
St George, Utah 84770
Ph (435) 656-0198
Fx (435) 688-9421
Toll Free (800) 909-3500

OGDEN
3340 S Harrison Blvd Ste
Ogden, Utah 84403
Ph (801) 392-9800
Fx (801) 392-9400
Toll Free (888) 786-2824

January 10, 2002

Edwin Erickson, CPA
HANSEN, BRADSHAW, MALMROSE & ERICKSON
261 East Broadway, Suite 100
Salt Lake City, UT 84111

150022607

Re: Madsen v Prudential- Aggregate Accounting

Dear Mr Erickson,

According to the Court's Order of January 2, 2002 (copy attached) you will now be performing the statistical computation for aggregate class damages Of course, the window for those computations (as ordered by Judge Rigtrup) will be March 3, 1971 to June 30, 1979.

However, we would like to remind you that the court has given us permission to have you preform an auxiliary computation of damages (at our expense) for the time period prior to March 3, 1971 and after June 30, 1979. (Motion, Memo and Order attached.) Also note from p. 2 and p 3 of the attached memorandum that we will be paying only the incremental increase in your fee for computing these damages.

Unless we hear from you to the contrary, we are assuming that you will be performing these auxiliary calculations at the same time as you prepare the core calculations for the years 1971 to 1979

Sincerely,

ROBERT J. DEBRY & ASSOCIATES

Robert J DeBry
Attorney

Attachments

cc Steven Tingey
Judge Burton

IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT

IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADDEN,	:	
Plaintiffs,	:	MEMORANDUM DECISION CASE NO. 750226073CV
vs.	:	HONORABLE ANNE M. STIRBA MARCY THORNE, COURT CLERK
PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION,	:	
Defendant.	:	

On January 9, 1998, the above-entitled matter came on for oral argument on several motions. At the hearing, the parties were represented by their respective counsel. The motions argued and submitted include the following: (1) Prudential's Renewed Motion to Decertify; (2) Prudential's Motion to Amend Bench Ruling; (3) Prudential's Amended Motion for Instructions to the Master; (4) Plaintiffs' Motion (and Second Motion) to Amend Conclusion of Law #5; (5) Plaintiffs' Motion to Amend Conclusion of Law #13 or Finding of Fact #15 and Prudential's Motion to Amend Conclusion of Law #10 and #13 and Finding of Fact #14 and #15; (6) Plaintiffs' Motion to Amend Conclusion of Law Based Upon New Case Law and Motion to Reopen the Trial for the Limited Purpose of Making Findings on Statute of Limitations Issue; (7) Plaintiffs' Motion for Order that Prudential is not Entitled to Any Reversion of Unclaimed Funds; and (8) Plaintiffs' Motion to Enlarge Class

Definition.

At the conclusion of oral argument, the Court took the motions under advisement. The Court has now carefully considered the motions, the written memoranda and exhibits supporting the motions, the arguments of counsel and the good cause that has been shown. Based upon the forgoing, the Court hereby enters the following ruling.

BACKGROUND

1. The Madsens are trustors as well as representatives of a certified class of borrowers. Prudential Federal Savings and Loan Association is both the trustee and the beneficiary under a deed of trust executed September 21, 1964, for the purpose of securing a promissory note in the sum of $16,800. The security conveyed was the home in which plaintiffs reside.

2. Plaintiffs, as the trustors, agreed to protect the security of Prudential by paying the insurance and taxes. In addition, they agreed to pay "budget payments" and pledge these additional amounts to the beneficiary as additional security for the full performance of the deed of trust and the note secured thereby.

3. Contending that the monthly budget payments under Provision 4 of their contract constitute a common law pledge, plaintiffs sought restitution of profits allegedly earned.

4. This action was tried in September 1985 before the

Honorable Kenneth Rigtrup. Judge Rigtrup entered Findings of Fact and Conclusions of Law in 1990. The case was tried only as to plaintiffs' claims individually, and the class claims were reserved.

5. On December 2, 1996, Judge Rigtrup entered his bench ruling concerning the definition of the purported class represented in this action.

6. On December 31, 1996, Judge Rigtrup retired from the bench. Subsequently, on April 21, 1997, the case was re-assigned by the presiding judge of the Third District Court to the undersigned.

7. On October 31, 1997, this Court entered Findings of Fact and Conclusions of Law as to the definition of the purported class represented in this action.

ANALYSIS

This case was initially filed in 1975: the year the undersigned judge started law school. The case is now nearly 23 years old.

Most of these current motions seek a reconsideration by this Court of several issues already decided by Judge Rigtrup and other judges a long time ago. Because of the extremely protracted nature of this case, the Court feels compelled to express its serious concern over the repeated attacks on legal issues that have been considered and decided previously (in some instances by more than

one judge).[1]

This approach is not the product of just one side of the dispute. Both sides have engaged in requests for reconsideration.[1]

Based upon the Court's consideration of the current motions, there is no adequate basis in law or fact for reconsideration of (1) Prudential's Renewed Motion to Decertify; (2) Prudential's Motion to Amend Bench Ruling; (3) Prudential's Amended Motion for Instructions to the Master; (4) Plaintiffs' Motion (and Second Motion) to Amend Conclusion of Law #5; and (5) Plaintiff's Motion to Amend Conclusion of Law #13 or Finding of Fact #15; and these motions are, consequently, denied.

Prudential's "Motion to Amend Conclusion of Law #10 and #13 and Finding of Fact #14 and #15," is hereby denied, except that Judge Rigtrup's award to plaintiffs of the simple interest at the annual rate of 10% on damages from the date of the conclusion of trial but prior to the entry of judgment, is hereby vacated on the ground a judgment is entered when the judgment is actually signed and entered, and an award of prejudgment is, therefore inappropriate.

As to Plaintiffs' "Motion to Amend Conclusion of Law Base Upon New Case Law and Motion to Reopen the Trial for the Limite

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[1]Although the parties contend that the law authorizes th Court to reconsider these issues, perhaps they ought to give mor consideration as to whether, in good judgment and conscience, ther ought to be a reconsideration.

Purpose of Making Findings on Statute of Limitations Issue," plaintiffs have failed to demonstrate that the use of the discovery rule is justified under Warren v. Provo City Corp., 838 P.2d 1125 (Utah 1992); and, therefore, there is no basis under Sevy v. Security Title, 902 P.2d 629 (Utah 1995), to amend the Conclusions of Law or to re-open the trial.

With regard to Plaintiffs' "Motion for Order that Prudential is not Entitled to Any Reversion of Unclaimed Funds," a ruling on this motion is deferred until such time as the Court considers other possibly competing claims on the judgment proceeds at the conclusion of the case. At this time, there are simply too many unknowns regarding the number of claimants, the amount owed to each, and the amounts to be disbursed, for this issue to be appropriately resolved. The notice to submit as to this motion is therefore hereby stricken. The motion may be re-submitted for decision at such time as the Court considers all other claims on the judgment proceeds.

Finally, the issues raised in Plaintiffs' "Motion to Enlarge Class Definition" are remanded to the Special Master for an assessment and recommendation, in accordance with the directives previously established by Judge Rigtrup, as to whether the class includes those parties in trust deed contracts identified as documents 12, 14 & 15 on Exhibit C of the Master's initial Report dated February 22, 1995. The Special Master shall file an

Hansen, Bradshaw, Malmrose & Erickson

A Professional Corporation
CERTIFIED PUBLIC ACCOUNTANTS

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801-296-0200
Fax 801-296-1218

March 1, 2002

750226073

Honorable Michael K. Burton
Third Judicial District Court
Salt Lake County, State of Utah

Dear Judge Burton:

This letter is our Report to the Court as required by the Court in its Order dated January 2, 2002. This Order specified the following:

> The Master shall, within 60 days of this order, produce to the Court a Report giving the Master's final statistical calculation of aggregate class damages. Furthermore for purposes of this report, if the mailing address and the property address are identical on the Mortgage Loan Master Reference Card (sample attached), the Master shall assume that such loans involve "primary residence", as that terms is used in prior Orders of the Court.

To accomplish this objective I met with Brad Slack at Washington Mutual to review the data base that he had prepared of the loan origination cards. This data base was prepared by Mr. Slack and other Washington Mutual Bank employees under his direction, as outlined in his August 7, 2000 affidavit filed with the Court. This process resulted in a data base of 14,482 loan cards. It should be noted that I have only performed a limited amount of testing of this data base, primarily in obtaining a sample of 50 loan cards to respond to plaintiff counsel's request of December 27, 2000. I have not yet performed testing to determine if all loan cards have been properly segregated between class members and non-members of the class. Based on the limited testing I have performed and based on my meetings and discussions with Mr. Slack, I have seen no evidence that the process of segregating the loan cards and developing the data base was not performed with due care.

The data base includes information regarding the mailing address of the borrower, as well as the property address as listed on each loan origination card. We requested that Mr. Slack print the entire data base and mark each borrower name where the loan address and property address did not agree. In performing this task, he also noted a third group of borrowers; those where it is not possible to determine if the mailing address and the property address are the same. There are two primary reasons for this classification; the first is when the property address is listed on the card but the mailing address is a P.O. box, the second is when a legal description of the property is listed as the property address. Mr. Slack marked this third category as well on the printout of the database.

After Mr. Slack completed the process of marking the data base printout for the three different categories, we obtained the printout from him. We tested the accuracy of his work by reviewing the printout and looking for any items which appeared to be improperly classified, based on the information listed. We found a small number of exceptions, and met with Mr. Slack to discuss the exceptions. He then made the appropriate corrections on the printout.

We then met again with Mr. Slack to sort the data base into the three categories:

1. Borrowers where the mailing address and property address agree.
2. Borrowers where the mailing address and property address did not agree.
3. Borrowers where it was indeterminable if the mailing address and property address agree.

As noted above, there were 14,482 total loans in the data base. This sorting process identified 10,796 loans in category 1, 3,192 loans in category 2, and 494 loans in category 3. Of the 10,796 loans in category 1 where the addresses match, there are 1,249 loans which are duplicated on the listing. Of the 494 loans in category 3, 30 are duplicate loans within the listing and an additional 57 are duplicates when compared to category 1. Duplication occurs primarily from assumption of the same loan by one or more subsequent borrowers. We considered whether duplicate loan numbers should be included in the estimate of aggregate damages and concluded they should be excluded. We arrived at this conclusion after considering the methodology used by Prudential in conducting its sample in 1993, from which we use data as described below in developing our estimate of aggregate damages. After subtracting the duplicate borrowers, the adjusted total of category 1 loans (where the property and mailing address match) was 9,547.

As discussed in our Report to the Court dated December 31, 1996, Prudential used the December 31, 1972 mortgage loan microfiche records as the population for its sample. For each of the 400 loans selected in its sample, Prudential obtained the annual statement summaries for the loan for each year from 1971 to 1979. The damage calculations were performed for the entire period the loan was outstanding from 1971 to 1979, whether the loan was assumed or not. Prudential's damage calculations for its sample were on a per loan basis, rather than per individual borrower.

As noted in our December 31, 1996 Report to the Court, the amount of damages for the 227 potential class loans from the sample totaled 23,875.69, or an average of $105.18 per class member or loan. For the purposes of this Report as directed by the Court, we believe this per loan sample average is meaningful and can be used to develop our estimate of aggregate damages, as follows:

Number of loans where property address and mailing address agree	9,547
Average damages per loan, from 1993 sample, for period March 3, 1971 to June 30, 1979	$ 105.18
Estimate of aggregate damages	$1,004,153

This aggregate damage estimate excludes any judgement interest subsequent to June 30, 1979.

If the category 3 or indeterminable loans were included in the above estimate, they would increase the estimate by a maximum of $42,808 if all of the non-duplicate total of 407 loans were found to be category 1 loans.

As previously noted, the completeness and accuracy of the data base has not been extensively tested. I would point out that the process used by Washington Mutual to develop this data base resulted in 9,547 loans identified, as described above. Our December 31, 1996 report to the Court arrived at an estimated 9,648 class members, based on the 1993 sample performed. The sample estimate of 9,648 is a close approximation of the 9,547 arrived at by individual examination of loan cards by Washington Mutual to prepare the data base, and provides additional evidence of the overall reasonableness of the class member size. While the exact number of class members may not be known at the present time, I believe we have a reasonable estimate of class member loans that can in turn be used to provide an overall estimate of aggregate damages.

The following are certain of the statistical parameters used by Prudential in their 1993 sample of 400 loans:

Population Estimate:

n	100
X-BAR	94.96
N	16,941
X-HAT	1,608,639

Confidence Interval Data:

Standard Deviation	118.42
Finite Correction Factor	0.99704
Standard Error	200,030
Reliability Level (Two-sided)	95%
Confidence Coefficient	1.96
Precision	392,059

Please contact me regarding any questions concerning the information in this letter.

Respectfully submitted,

Edwin Erickson

Edwin L. Erickson, CPA

ELE:cp

Hansen, Bradshaw, Malmrose & Erickson

A Professional Corporation

CERTIFIED PUBLIC ACCOUNTANTS

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September 12, 2003

Honorable L A Dever
Third Judicial District Court
450 South State Street
Salt Lake City, UT 84114

RE Madsen vs Prudential
Civil No C79-8404
Trial No 750226073

Dear Judge Dever

This letter is in response to Plaintiff's motion that the Court order the Master to Appear and Show Cause why he Should not be Held in Contempt of Court dated July 10, 2003, and to Plaintiff s Reply to Prudential's Memorandum in Opposition to Madsens' Motion that Special Master Show Cause Why He Should Not be Held in Contempt, dated August 27, 2003

I apologize to the Court for not responding sooner, I mistakenly assumed the Court would order me to appear and respond to the original motion if deemed necessary by the Court

To prepare my response, I have obtained and reviewed the May 30, 2003 and August 26, 2003 affidavits of Andrew Carr Conway, Jr , as well as defendant's Memorandum in Opposition to Madsens' Motion that Special Master Show Cause Why He Should Not be Held in Contempt dated August 4, 2003

It appears the main arguments presented by Mr Conway and plaintiff's counsel is that I have not followed professional standards and that I have tried to deceive the Court Specifically, they allege my use of "negative assurance' in my March 1, 2002 Report to the Court violates certain Generally Accepted Auditing Standards (GAAS) they believe are applicable to the work I have performed as Special Master They also allege deceit on my part for not disclosing that my report violated professional standards, as well as for claiming that I had performed a limited amount of testing of the loan card data base My response to these allegations follows

Alleged Violation of Professional Standards

Mr. Conway, on page 3 of his August 26, 2003 affidavit, states his professional opinion is that "the requirements within the professional literature for consulting engagements are parallel to those in the 'audit literature' ". He concludes that "sufficient relevant data" under Consulting Services Standards is similar or even parallel to evidential matter as discussed in GAAS (AU Section 326). He concludes in paragraph 11 that my use of "negative assurances" in my March 1, 2002 Report are improper and violate GAAS and/or Consulting Services Standards. On page 2 of his affidavit, he also questions the ability of Mr. Tingey and Ms. Maragakis to make judgments about "what constitutes an audit" as recognized by the accounting profession.

For the record, I have been a CPA for over 25 years. I have worked almost exclusively as an audit staff member, senior, manager, senior manager and partner for two national CPA firms and for a local CPA firm. I have also taught audit courses at the university level for two years. Based on my experience and background, let me state clearly THIS ENGAGEMENT IS NOT AN AUDIT. Mr. Conway's criticisms of my using negative assurances are based on prohibitions of using such assurances in expressing an audit opinion. He also states in his May 30, 2003 affidavit on page 12 that "such language is called 'negative assurance' and is generally viewed with disapproval by the accounting profession except in certain very limited circumstances". I disagree that this language is viewed "with disapproval" and only used in "very limited circumstances". A few examples will suffice.

When CPAs issue a review report on financial statements under AICPA Statements on Standards for Accounting and Review Services, they are required to use negative assurance, i.e., "We are not aware of any material modifications that should be made to the accompanying financial statements ...". Similarly, when a CPA reports on compliance with contractual provisions or regulatory requirements related to audited financial statements, he is required to "provide(s) negative assurance relative to compliance with the applicable covenants of the agreement insofar as they relate to accounting matters, and specify that the negative assurance is being given in connection with the audit of the financial statements". (AU 623, para 20 (c)). Finally, when CPAs issue "comfort letters" to underwriters in connection with unaudited financial statements included in public offerings, they are "limited to providing negative assurance on compliance as to form and content of financial statements..." (AU 634.34). I believe these examples clearly demonstrate negative assurance is commonly used and not "viewed with disapproval by the accounting profession".

As for my reason for using negative assurance in my March 1, 2002 Report, I clearly felt this was the most appropriate and descriptive language, given the limited amount of work I had performed to that point. I was careful to point out, both on page 1 and page 3 of my Report, that the loan data base had not been extensively tested. Based on the testing I had performed, I felt it would have been irresponsible of me to express positive assurance that all loan cards had been properly segregated. Remarkably, plaintiff's counsel confuses the issue of my providing negative assurance in my Report to falsely stating in their August 27, 2003 Memorandum "he (the Master) relied on 'negative assurances' from officers of Prudential in preparing that March 1, 2002 Report." I assume this misstatement was an honest mistake on Counsel's part and not "deceit"!

At this point, a little background may be helpful. In the hearing before Judge Burton on January 2, 2002, and in previous motions before the Court, there was discussion of whether class damages would be calculated on an individual or aggregate basis. Judge Burton ordered a "statistical calculation of aggregate class damages" using certain criteria to define class members. Also, both sides in this case have repeatedly made reference to "certain appeals" of the Court's final decisions. It seemed the Court's interest and intent was to obtain an estimate that could be used as a step to help expedite a resolution of the case. As I stated in my letter to Mr. DeBry of April 23, 2003 (see Exhibit A attached) in paragraph 4, "of course, as this matter progresses to the

point where damages are distributed to class members, we will perform additional testing to confirm proper identification of class members and completeness of the data base". I concluded and still believe that the work performed was sufficient to provide the Court with a reasonable estimate upon which to make further decisions. As I noted in my March 1, 2002 Report, the data base consists of 9,547 loans identified, which is a close approximation of the 9,648 estimated number based on sampling procedures described in my December 31, 1996 Report to the Court. As I stated then, I believe the comparability of these two numbers provides additional evidence of the overall reasonableness and accuracy of the class member size.

Alleged Deception of the Court

The second issue presented by plaintiff's counsel and Mr. Conway is that I attempted to deceive the Court by stating I had performed a limited amount of testing in relation to the loan cards. As you are aware, at the request of plaintiff's counsel, I went to Prudential offices in December 2000 where the loan cards are kept. I discussed with Mr. Slack the process he and his staff followed to segregate the loan cards between potential class and non-class members. I obtained copies of 50 loan cards which I selected at random. I obtained 33 cards included in the class, 17 cards which had been excluded. These loan cards contain information which identify whether they are conventional, FHA, VA, or other types of loans. Based on obtaining this sample of loan cards, and my discussions with Mr. Slack, I believed it appropriate to state I had "performed a limited amount of testing". Mr. Conway's August 26, 2003 affidavit does not dispute whether I performed any testing, but instead states "I can see absolutely no way that an examination of fifty loan cards from a total universe of 70,000 loan cards, could in any way be referred to as a 'limited amount of testing' sufficient to meet the standard of 'sufficient relevant data' in the Consulting Services Standards" (emphasis added). I partially agree with Mr. Conway that the limited testing performed may not meet a higher standard of evidential matter in an audit engagement, however, I never have claimed to have performed sufficient test work to meet such a standard. I have consistently stated the opposite, that only a limited amount of testing had been done and more testing would be required!

In conclusion, I strongly believe I have not violated professional standards and have not made any effort to deceive the Court in any way.

Respectfully submitted,

Edwin Erickson

Edwin L. Erickson, CPA

ELE:cp

cc: Stephen Tingey
Joseph Palmer
Robert DeBry

April 23, 2003

Mr. Robert J. DeBry
Robert J. DeBry & Associates
4252 South 700 East
Salt Lake City, UT 84107

Dear Bob:

Your letter of April 8, 2003 asks six questions. My response is as follows:

1. Difference between sample size of 400 and n-100. The original sample selected by Prudential was 100 items, generated on November 25, 1993. On January 5, 1994, an expanded sample of 400 loans was generated. My recollection of the reason to increase the sample from 100 to 400 was due to the fact many of the loans selected from the microfiche were not potentially class members, since they were FHA, VA, construction, etc. type loans. The larger sample was necessary to obtain a representative number of conventional mortgages that would be potential class members. The statistical parameters quoted on page 3 of my March 1, 2002 report are based on the original sample of 100 which was subsequently increased to 400. The parameters for the sample of 400 are discussed in question 2 below.

2. Estimate of aggregate damages of $1,004,152 per March 1, 2002 report versus X-HAT of $1,608,639. As discussed above, Prudential's original statistical estimate based on a sample of 100 resulted in an estimate of $1,608,639, with a precision of $392,059, resulting in an estimate range of $1,216,581 to $2,000,698 (See copy of sample summary sheet attached). This sample summary includes an interest component on the damages as well. As noted in our December 31, 1996 report, the interest component at 10% was $119.21 per class member, compared to damages of $105.18 per class member. As noted in the December 31, 1996 report, our total damage estimate (including interest) was $2,164,915. This amount compares to Prudential's statistical estimate of $1,888,070, with an estimated range of $1,675,577 to $2,100,563 (see iteration #6 on attached sample summary). The main difference between the sample estimate of $1,004,152 and the higher amounts estimated by Prudential and by myself is the interest component, which was excluded based on instructions from the Court for my March 1, 2002 report.

3. Precision of $392,059 and X-HAT of $1,608,639. As discussed above, these sample parameters for the sample of 100 were picked up in error. The parameters should have been a precision of $212,493 and an X-HAT of $1,888,070, based on the larger sample of 400.

4. Testing of 14,482 data base of loan cards. In my March 1, 2002 report to the Court, I stated,"I have not yet performed testing to determine if all loan cards have been properly segregated between class members and non-members of the class". As indicated in my December 27, 2000 letter to you, I met with Mr. Slack at that time and reviewed with him the process he followed to segregate the loan cards. He represented to me that he followed the criteria established by the Court in determining class members. Of course, as this matter progresses to the point where damages are distributed to class members, we will perform additional testing to confirm proper identification of class members and completeness of the data base.

5. Request for data supporting average damage per loan of $105.18. I apologize for not responding to this request. I thought Mr. Shaha obtained this information when he met with Washington Mutual representatives and reviewed the sample. I have attached a copy of the five pages of the sample results. The totals at the bottom of the fourth page agree to our December 31, 1996 report. The fifth page totals include nonowner occupied loans such as thrift and loan entities, etc. which were excluded. As in the past, I have covered the names of the borrowers to preserve confidentiality.

6. Testwork performed on Prudential sample. To test the sample performed by Prudential, we tested every 20th loan in the sample, or 20 loans. For these 20 loans, we obtained the microfiche designated by the random number generator program and verified the proper loan was selected. We then obtained copies of the annual statement summaries for each of the 20 loans for each year end from 1971 to 1979 for which the loan had activity. We then entered the monthly escrow balances into a spreadsheet, using the formulas established by the Court for the Madsen loan. We then compared the total damages, including interest, from our spreadsheet for these loans to the amount listed by Prudential in its sample summary. As discussed previously, we found two minor errors, one which changed the sample total slightly by $6.44. We revised the sample total prepared by Prudential by the $6.44 and concluded we could rely on the accuracy of the sample work performed by Prudential.

Sincerely,

Edwin L. Erickson, CPA

cc: Stephen Tingey, Esq.
Joseph Palmer, Esq.
Honorable L.A. Dever

Enclosures

IN THE THIRD JUDICIAL DISTRICT COURT
IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiff, v. WASHINGTON MUTUAL BANK fsb (successor to PRUDENTIAL FEDERAL SAVINGS and LOAN ASSOCIATION), Defendant.	**FINAL JUDGMENT** # 7502260 73 Civil No. C79-8404 Honorable L. A. Dever

It is hereby ordered, adjudged, and decreed that:

1. Judgment is entered against defendant Washington Mutual Bank fsb, successor to Prudential Federal Savings and Loan Association in the amount of $1,004,153 as the total lump sum damages and in favor of Nancy Madsen, in her capacity as representative of a certified class of persons, similarly situated, consisting of the borrowers on the 9,547 loans identified by the Special Master comprising a class defined as borrowers (i) whose loan include a trust deed containing the pledge language as in the Madsens' Trust Deed, as identified by the Special Master; (ii) who had any funds in escrow reserve budget accounts between March 3, 1971 and June 30, 1979; (iii) whose loan was for a single-family, owner-occupied, residential primary residence; (iv) whose loan originated in Utah; and (v) whose mailing address and property address are identical on the Mortgage Loan Master Reference Card, thereby establishing "primary residence." The actual names of class members can be provided to the appellate court by supplemental filing if so desired or requested by the appellate court.

2. The amount of the foregoing aggregate judgment to be received by class members for each loan within the class is the cumulative net earnings on the average escrow balance for that class member's loan, compounded for the period March 3, 1971 to June 30, 1979, arrived at by applying the following "net yield" for each year:

1971	3.17%
1972	2.97%
1973	6.01%
1974	6.76%
1975	4.59%
1976	3.20%
1977	3.95%
1978	5.94%
1979	8.89%

less attorneys' fees awarded to plaintiffs' counsel in the amount of 33.3% of the foregoing.

3. Defendant Washington Mutual Bank fsb shall pay post-judgment interest, at the rate set forth in Utah Code Ann. § 15-1-4, from the date of this Judgment, until the amount of the aggregate is deposited in court, in cash or bond.

4. Defendant Washington Mutual Bank fsb shall pay plaintiffs' costs to the extent required by Utah Rule of Civil Procedure 54, and as determined by the Court, in the amount of _____.

DATED May 31, 2006.

BY THE COURT:

Honorable [illegible] Dever

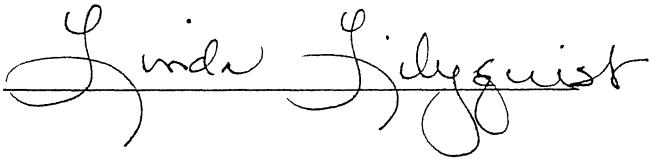
STATE OF UTAH THIRD DISTRICT COURT SALT LAKE CITY

1-2442

CERTIFICATE OF SERVICE

I certify that on June 19th, 2005, a true and correct copy of the foregoing proposed **FINAL JUDGMENT** was hand-delivered to the following:

Robert J. DeBry
DEBRY & ASSOCIATES
4252 South 700 East
Salt Lake City, Utah 84107



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INTEREST ON MORTGAGE LOAN ACCOUNTS ACT
(§ 7-17-1 *et seq.* U.C.A., as amended by 1985)

7-17-1. Legislative intent.

It is the intent of the Legislature that the provisions of this act govern the rights, duties and liabilities of borrowers and lenders with respect to reserve accounts established before and after the effective date of this act.

7-17-2. Definitions.

As used in this chapter:

(1) "Real estate loan" means any agreement providing for a loan secured by an interest in real estate in this state containing a residential structure of not more than four housing units, at least one of which is the primary residence of the borrower and includes, but is not limited to, agreements secured by mortgages, trust deeds, and conditional land sales contracts.

(2) "Borrower" means any person who becomes obligated on a real estate loan at the time of origination of such loan and includes mortgagors, trustors under trust deeds and vendees under conditional land sales contracts.

(3) "Lender" means any person who regularly makes, extends or holds real estate loans and includes, but is not limited to, mortgagees, beneficiaries under trust deeds and vendors under conditional land sales contracts and who regularly require or maintain reserve accounts.

(4) "Person" includes an individual, a commercial bank, savings bank, building and loan corporation, savings and loan association, credit union, investment company, insurance company, pension fund, mortgage company, trust company, or any other organization making real estate loans.

(5) "Reserve account" means any account, whether denominated escrow, impound, trust, pledge, reserve or otherwise, which is established in connection with a loan secured by an interest in real estate located in this state, whether or not a real estate loan as defined in this chapter, and whether incorporated into the loan agreement or a separate document, whereby the borrower agrees to make periodic prepayment to the lender or its designee of taxes, insurance premiums or other charges pertaining to the property securing the loan and the lender or its designee agrees to pay the taxes, insurance premiums or other charges out of the account on or before their due date.

(6) "Service charge" means any direct fee imposed in connection with the administration of a reserve account.

(7) A loan is "made" when the lender makes its initial disbursement of the loan proceeds.

7-17-3. Lender to pay interest -- Exceptions -- Computation -- Time for payment -- Service charges prohibited -- Written agreement.

(1) Each lender requiring the establishment or continuance of a reserve account in connection with an existing or future real estate loan shall pay interest on funds deposited in the account of at least 5 1/4% simple interest per annum, unless:

(a) The reserve account is required by a governmental insurer or guarantor of the loan as a condition of insurance or guaranty;

(b) The reserve account is maintained in connection with a real estate loan in an original principal amount exceeding 80% of the lender's appraised value of the property at the time the loan is made provided that when the principal balance of the loan is paid down to 80% this exception shall not apply; or

(c) The payment of interest or other compensation to the borrower for the use of funds deposited in a reserve account is prohibited by federal law or regulations.

(2) The interest shall be computed as of the end of the calendar year on the average of the month end balances in the account for that calendar year or partial calendar year, except that in the event of payoff of the real estate loan, interest shall be computed on the average month end balances in the account for the partial year ending at the end of the month preceding payoff. The interest shall, within 60 days after the end of each calendar year, at the election of the lender, be credited to the remaining principal balance on the loan, paid to the borrower, his successors or assigns, or credited to the reserve account, except that in the event of payoff of the real estate loan, the interest shall be paid or credited to the borrower, his successors or assigns within 30 days after the date of payoff.

(3) No lender shall require or impose a service charge for the administration of a reserve account.

(4) Except as provided in this section, no lender shall be obligated to pay interest on or account for the earnings from funds in any reserve account in connection with the real estate loan made or held after June 30, 1979, unless an agreement in writing expressly so providing was executed by the borrower and lender.

7-17-4. Options in lieu of reserve account -- Notice by lender -- Selection by borrower -- Noninterest-bearing reserve account.

(1) A lender not requiring the establishment and maintenance of a reserve account shall offer the borrower the following options:

(a) The borrower may elect to maintain a non-interest-bearing reserve account to be serviced by the lender at no charge to the borrower; or

(b) The borrower may manage the payment of insurance premiums, taxes and other charges for his own account.

(2) The lender shall give written notice of the options to the borrower: (i) with respect to real estate loans existing on the effective date by notice mailed not more than 30 days after the effective date; (ii) with respect to real estate loans made on or after the effective date by notice given at or prior to the closing of the loan. The notice shall clearly describe the options and state that a reserve account is not required by the lender, that the borrower is legally responsible for the payment of taxes, insurance premiums and other charges and that the notice is being given pursuant to this act. For real estate loans in existence on the effective date the borrower must select one of the options prior to 60 days after the effective date. If no option is selected prior to 60 days after the effective date the borrower will be deemed to have selected option (a), provided, however, that the borrower at a later time may select option (b). For loans made on or after the effective date the borrower shall select one of the options at the closing. If the borrower selects option (a), the lender shall not be required to account for earnings, if any, on the account.

(3) If the borrower who selects option (b), or his successors or assigns, fails to pay the taxes, insurance premiums or other charges pertaining to the property securing the loan prior to the delinquency date for such payments, the lender may require a reserve account without interest or other compensation for the use of the funds; provided, that the lender may not require a reserve account without interest or other compensation if (a) the borrower pays any delinquency within 30 days and (b) the borrower has not previously been delinquent in payment of taxes, insurance premiums or other charges.

7-17-5. Statements.

Every lender shall furnish to the borrower, or his successors or assigns, without charge, within 60 days after the end of each calendar year, an itemized statement showing moneys (1) received for interest and principal repayment and (2) received and held in or disbursed from a reserve account, if any.

7-17-6. Liability of lender for failure to pay taxes, insurance premiums or other charges.

A lender administering a reserve account shall make timely payments of taxes, insurance premiums and other charges for which the account is established, if funds paid into the account by the borrower, his successors or assigns, are sufficient for the payments. Negligent failure to make the payments required for taxes, insurance premiums and other charges as they become due, from available funds in the reserve account, shall subject the lender to liability for all damages directly resulting from the failure; provided that this sentence shall not deprive the lender of the right to present any defense it may have in any action brought to enforce the liability. Failure of the borrower or his successors or assigns to deliver promptly to the lender all notices of tax assessments and insurance premiums or other charges, received by the borrower, his successors or assigns, shall relieve the lender from liability under this section.

7-17-7. Limit on amount borrower required to pay into account -- Deficiency -- Method of recouping and remedies for default.

No lender in connection with a real estate loan shall require a borrower, his successors or assigns, or a prospective borrower:

(1) to deposit in any reserve account established in connection with the loan, prior to or upon closing, a sum exceeding the estimated total payments for taxes, insurance premiums or other charges which will be due and payable on the date of closing, and the pro rata portion thereof which has accrued, plus 1/12th of the estimated total taxes, insurance premiums and other charges which will become due and payable during the 12-month period beginning on the date of closing; or

(2) to deposit in any reserve account in any month beginning after closing a sum exceeding 1/12th of the total estimated taxes, insurance premiums, or other charges which will become due and payable during the 12-month period beginning on the first day of the month, except that:

(a) If the lender determines there will be a deficiency on the due date, it may require additional monthly deposits in the reserve account of pro rata portions of the deficiency corresponding to the number of months from the date of the lender's determination of the deficiency to the date upon which the charges become due and payable;

(b) If the lender determines there is a deficiency on or after the due date, it may bill the borrower, his successors or assigns, for the deficiency, which bill shall promptly be paid, or pay the deficiency, add that amount to the principal, or charge the reserve account, and require additional monthly deposits in the reserve account over the next 12 months to

recoup the deficiency. If the borrower, his successors or assigns, fails to pay any amount billed by the lender to meet the deficiency, the lender may exercise any remedies for default contained in the real estate loan document. If such failure to pay continues for 30 days after written notice to borrower, the lender may also terminate any obligation to pay interest or to otherwise pay compensation for the use of the funds in the reserve account.

7-17-8. Damages for lender's violation of act -- Limitations on recovery.

(1) Except as otherwise provided in this act, a lender who violates this act is liable to the borrower, his successors or assigns, for the actual damages suffered by the borrower, his assigns or successors, or $100, whichever is greater. If an action is commenced, the prevailing party may be awarded reasonable attorney's fees as determined by the court.

(2) A lender has no liability under this section if the court finds that written demand for payment of the claim of the borrower, his successors or assigns, was made on the lender not less than 30 days before commencement of the action and that the lender tendered to the borrower, his successors or assigns, prior to the commencement of the action, an amount not less than the damages awarded.

(3) A lender may not be held liable under this section for a violation of this act if the lender shows that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures to avoid such errors.

(4) A reserve account established or maintained in violation of this act is voidable, at the option of the borrower, his successors or assigns, at any time, but shall not otherwise affect the validity of the loan, the security interest in the real property or any other obligation of the borrower.

(5) No action under this section may be brought more than one year after the date of the violation.

7-17-9. Actions on accounts established prior to 1979 -- Limitations on recovery.

(1) With respect to any reserve account established prior to July 1, 1979 and for which no legal action is pending as of January 1, 1979, no recovery shall be had in any action brought to require payment of interest on, or other compensation for, the use prior to July 1, 1979, of the funds in such account unless:

(a) An agreement in writing expressly so providing was executed by the borrower and the lender; or

(b) The borrower, or his successors or assigns, establishes by clear and convincing evidence an agreement between the parties that the lender would pay interest on or to otherwise compensate the borrower for the use of the funds in such account. Use in the loan documents of such words as "trust"or "pledge" alone shall not establish the intent of the parties; and

(c) There is no federal law or regulation prohibiting the payment of interest on or otherwise compensating the borrower for the use of the funds in such an account.

(2) No action seeking payment of interest on or other compensation for the use of the funds in any reserve account for any period prior to July 1, 1979, shall be brought after June 30, 1981. Any recovery in any such action shall be limited to the four-year period immediately preceding the commencement of the action. No recovery shall be had in respect of any reserve account established prior to July 1, 1979 greater than if the provisions of Section 7-17-3 of this act were applicable to such accounts.

(3) With respect to any reserve account established prior to July 1, 1979, an agreement in writing between the lender and the borrower, or his successors or assigns, that (a) the provisions of Section 7-17-3 of this act shall apply to all payments made subsequent to July 1, 1979, or (b) the borrower may exercise, for the period subsequent to July 1, 1979, either of the options provided in Section 7-17-4 of this act, shall bar any recovery by the borrower, his successors or assigns, for interest on or other compensation for the use of the funds in such account for any period prior to July 1, 1979.

7-17-10. Applicability of act to accounts and actions thereon.

The provisions of this act shall apply:

(1) to all reserve accounts; and

(2) to all actions filed after January 1, 1979, to recover interest on or other compensation for the use of the funds in any reserve account whether or not the reserve accounts were established prior to or subsequent to July 1, 1979.